

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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<i>In re Consolidated Application of</i>)	
)	
EchoStar Communications Corporation,)	
General Motors Corporation,)	
Hughes Electronics Corporation,)	
)	
Transferors,)	
)	
and)	CS Docket No. 01-348
)	
EchoStar Communications Corporation,)	
)	
Transferee,)	
)	
For Authority to Transfer Control.)	
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PEGASUS COMMUNICATIONS CORPORATION'S PETITION TO DENY

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SUMMARY

The Proposed Merger –

This proceeding presents a simple question:

Is it in the public interest to allow DIRECTV and EchoStar, the only facilities-based DBS providers in the United States today, to cease competing with each other and instead combine their services in one monopoly provider?

The Argument of the Transfer Applicants –

The transfer applicants do not deny that the object of their merger is the creation of a monopoly in DBS and satellite broadband. Instead, following the principle that a good offense is the best defense, they argue without apparent embarrassment that the creation of a formidable satellite monopoly will *increase* competition in the provision of multichannel video and broadband services in the United States. In doing so, they do not seek to deny that the proposed monopoly (New EchoStar) will amass in one company an unprecedented – and daunting – array of assets, including:

- 1) 100% of the BSS Ku-band satellite slots licensed to the United States that allow coverage of the entire continental United States (“CONUS”);
- 2) Through ownership or an exclusive distribution relationship, 100% of the 17 million U.S. DBS multichannel video subscribers (thereby making New EchoStar the largest cable or satellite company);
- 3) Approximately one-third of the FSS Ka-band satellite slots licensed to the United States that allow CONUS coverage and which are necessary for the provision of competitive satellite broadband services (no other U.S. licensee would hold more than 5% of U.S. CONUS Ka licenses.); and
- 4) Ownership of 100% of the technologies currently available that are necessary for delivery of satellite broadband services to consumers.

Instead, the transfer applicants argue that the creation of a *national* satellite *monopoly* is necessary to enable the direct to home satellite services industry to compete

effectively with regional and local cable companies that, without exception, are smaller – most far smaller – than the proposed satellite monopoly. Distilled to its simplest expression, the transfer applicants are advancing an audacious proposition that the exercise of unchecked monopoly power by New EchoStar will better serve the public interest than the checks and balances of a competitive marketplace.

The Burden of Proof Lies with the Transfer Applicants –

The transfer applicants bear the burden of proving their arguments that the merger is in the public interest and that it would enhance competition. However, beyond their bold and counter-intuitive assertions that the creation of a monopoly will enhance competition, they have provided virtually no evidence that this merger will – or is necessary to – produce the benefits they assert. The preponderance of the “efficiencies” they identify are cost savings that result from the elimination of competition between them. Notably, they have neither demonstrated nor committed that these cost savings will inure to the benefit of consumers. Indeed, they have communicated clearly and publicly to the financial markets that most of those savings will inure to shareholders – to General Motors at consummation of the proposed merger through an extraordinary \$4.2 billion cash dividend and, over time, to the remaining shareholders of New EchoStar.

The transfer applicants claim that the public will benefit from the cessation of competition between them because, by combining their unique Ku-band CONUS authorizations and facilities, they will be able to eliminate duplicative carriage of programming and services. They assert that this elimination of duplicative carriage is necessary to free-up capacity in order to add national and local programming not currently offered by either DIRECTV or EchoStar. However, the transfer applicants have

failed to provide any evidence that the spectrum currently licensed to them is not adequate to enable them to compete effectively. Rather, they simply have advanced the mathematically unassailable proposition that, a monopolist's use of one channel to carry what two competitors previously used two channels to carry, will free-up one channel. But that begs the real question: Do the transfer applicants need to merge in order to have sufficient capacity to compete effectively? As demonstrated in this Petition, the answer to that question is **NO**. Each of the transfer applicants already has sufficient capacity, and through the use of existing technologies they each could increase their capacity even more. They will have a strong incentive to continue to innovate if they remain competitors. The merger would eliminate that incentive.

The transfer applicants also claim that the merger is necessary for them to provide satellite broadband service and to bundle broadband with their DBS video services so that they can compete effectively with digital cable systems that also bundle multichannel video with broadband. Leaving aside the fact that such cable systems are hardly ubiquitous, that there appears to be a slowdown in their deployment even in urban and suburban areas, and that there is little if any likelihood that they will ever be deployed extensively in rural areas, the transfer applicants have failed to demonstrate why the merger is necessary to enable satellite broadband services to be bundled with existing DBS services, particularly since EchoStar and DIRECTV are both already doing so today. Moreover, the transfer applicants do not explain why, if they are correct, the creation of a monopoly DBS provider will not inevitably eliminate *any* prospect of independent, stand-alone satellite broadband companies emerging to compete with satellite broadband services offered by the DBS monopolist.

Finally, the transfer applicants repeatedly rely on the absence of any vertical integration strategy as one of the key benefits of the proposed transaction. Of course, the credibility of that alleged benefit has been seriously, if not completely, undermined by EchoStar's recently consummated relationship with Vivendi.

Pegasus' Petition to Deny –

Pegasus Communications Corporation ("Pegasus") offers a simpler and more intuitively obvious assessment of the proposed merger. The creation of a monopoly is presumptively anti-competitive. In this instance, the proposed merger will eliminate the vibrant competition that has characterized the DBS industry since its inception seven years ago, and also will ensure that competition in the nascent satellite broadband industry will be snuffed out at birth.

This merger is in direct opposition to virtually all of the principles that have framed Commission policies with regard to the direct to home satellite services industry over the last decade. It is also unambiguously contrary to U.S. antitrust law and policy. It is clearly and unmistakably **NOT** in the public interest. Indeed, the merger is manifestly antithetical to the public interest. The Commission should therefore deny the transfer application outright in order to ensure that robust competition continues – with two viable facilities-based providers – each with a strong incentive to innovate and improve their service, for the benefit of all consumers.

Pegasus is Uniquely Situated to Comment –

Pegasus is intimately familiar with DBS and satellite broadband, as well as with over-the-air television and cable. Its mission is the provision of television, multichannel video and broadband access to rural and underserved communities.

Pegasus (through certain of its subsidiaries) is the exclusive distributor of DIRECTV in rural areas encompassing almost 8 million households. Pegasus currently provides DBS service to approximately 1.5 million rural households in 41 states – almost 10% of all U.S. DBS subscribers. Pegasus’ penetration of 20% of its rural service areas is the highest of any DBS provider in North America, and is higher than the cumulative penetration of DIRECTV and EchoStar nationwide. Pegasus is also a nationwide distributor of Pegasus Express, a satellite broadband service powered by the DIRECWAY satellite broadband technology developed by Hughes Network Systems. Pegasus owns or operates eleven television stations, none of which is currently re-transmitted by DIRECTV or EchoStar. Until two years ago, Pegasus also operated cable systems serving rural and underserved communities. Pegasus has experienced exceptional growth since the launch of the first DBS service, growing from a private company with annual revenues of less than \$40 million in 1996, to a publicly traded company generating almost \$900 million in annual revenues today.

Pegasus and its stakeholders – its present and future customers, shareholders and employees – have a keen understanding of the issues presented by this transfer and a direct interest in the outcome of this proceeding.

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PEGASUS COMMUNICATIONS CORPORATION'S PETITION TO DENY

Pegasus Communications Corporation ("Pegasus"), pursuant to the Public Notice released by the Federal Communications Commission (the "Commission" or "FCC") on December 21, 2001,¹ respectfully petitions the Commission to deny the pending consolidated transfer of control application ("Application") in this proceeding.²

¹ *EchoStar Communications Corp., General Motors Corp., and Hughes Electronics Corp. Seek FCC Consent for a Proposed Transfer of Control*, Public Notice, CS Dkt No. 01-348, DA 01-3005, 2001 WL 1636540 (Dec. 21, 2001) ("Public Notice").

² In support of this Petition, Pegasus is filing herewith: (i) the affidavit and report of Daniel L. Rubinfeld, the Robert L. Bridges Professor of Law and Professor of Economics at the University of California, Berkeley, and former Deputy Assistant Attorney General at the Antitrust Division of the U.S. Department of Justice ("Rubinfeld Aff."), contained in Attachment A; (ii) the affidavit and report of Roger J. Rusch, a professional telecommunications engineer who specializes in communications and broadcast satellite systems, who is the President of TelAstra, Inc., a technical and management-consulting firm located in Palos Verdes, California ("Rusch Aff."), contained in Attachment B; and (iii) other supporting materials, contained in Attachment C.

INTRODUCTION

As explained in the foregoing Summary, Pegasus has a direct interest in the outcome of this transfer proceeding.

Pegasus' familiarity with the preferences of, and limited options available to, rural consumers, gives it a unique vantage point from which it can appreciate the particularly adverse impact of the proposed EchoStar/DIRECTV merger on rural America. Rural households represent one third of all households in the United States. From the earliest days of television, rural consumers have been the last to receive video and other services. Moreover, because rural Americans frequently are underserved – and, in many cases, not served – by cable, they often do not benefit from the same multichannel video programming competition as urban and suburban residents. DIRECTV recently reported to the Commission that only 71% of its subscribers have access to cable.³ Pegasus, which distributes the DIRECTV service in rural areas, estimates that approximately 30% of its customers have no cable access, and fewer than 10% have access to digital cable. As the following chart illustrates, as many as 24 million U.S. housing units may not be served by cable systems.⁴

³ See Comments of DIRECTV, *In re Annual Assessment of the Status of Competition in the Markets for the Delivery of Video Programming*, CS Dkt No. 01-129 (Aug. 3, 2001), at p. 13 (“*DIRECTV 01-129 Comments*”).

⁴ Sources for this chart include: (1) United States 2000 Census, *available at* <http://www.census.gov/main/www/cen2000.html>; (2) 69 Television and Cable Factbook (Albert Warren ed., Warren Pub. Inc.) (2001) (“2001 Warren Cable Factbook”); (3) National Telephone Cooperative Association (NTCA), *NTCA 2001 Internet/Broadband Availability Survey*, as published in the Nov. 11, 2001 Skyreport (data as of Sept. 30, 2001); and (4) EchoStar and DIRECTV subscribers as reported by the companies as of Sept. 30, 2001.

head-to-head competition for rural subscribers, DBS fulfilled that function admirably, offering unserved rural residents hundreds of channels of programming and other services at affordable prices. Prior to EchoStar's entry, DBS customer equipment cost up to \$1,000; today, the equipment costs are often \$50 or less.

Satellite is also the most promising means by which rural Americans can obtain broadband services. As explained below, rural communities often are too dispersed to support DSL service, and cable modems require upgrades to the cable plant which are exceedingly unlikely to occur in much of rural America. Thus, as was the case for multichannel video programming, the availability of broadband at reasonable costs is dependent upon competition among satellite providers, which would be eliminated by the proposed merger.

In light of Pegasus' diverse experience with the technical, business and competitive issues at the core of this proceeding, it is well situated to provide insight into the fundamental questions raised, and policies implicated by, the proposed transfer of control, and to evaluate comprehensively the public interest ramifications of an EchoStar/DIRECTV merger. As explained in detail in the following sections, the proposed transfer of control raises profound public interest concerns with respect to the provision of satellite video programming, satellite broadband service, and a bundled satellite service offering these and other features.⁶ The transfer applicants' efforts to

Footnote continued from previous page

urban counties, defined by Nielsen as "A" or "B" counties. Thus, the remaining half reside in rural ("C" and "D") counties. *See DIRECTV 01-129 Comments* at 11-12.

⁶ Of the comments filed in this proceeding to date – mostly by consumers – the overwhelming majority have opposed the proposed transfer of control.

explain away these harms by pointing to alleged “efficiencies” and what are, at best, speculative benefits, are unavailing. They do not come close to offsetting the dramatic anti-competitive consequences of the proposed merger, especially for rural Americans.

DISCUSSION

I. The Transfer Applicants Must Prove By A Preponderance Of The Evidence That The Transfer Of Control Will Serve The “Public Interest, Convenience And Necessity” And That It Will Enhance Competition

In order to approve the consolidated transfer of control application, the Commission must find, pursuant to Sections 214(a) and 310(d) of the Communications Act of 1934, as amended (the “Communications Act”), that the proposed transfer of control would serve the public interest.⁷ In making this determination, the Commission “weigh[s] the potential public interest harms of the proposed transaction against the potential public interest benefits to ensure that the Applicants have demonstrated that, on balance, the merger serves the public interest and convenience.”⁸ “The Applicants bear the burden of proving by a preponderance of the evidence that, on balance, the proposed transaction serves the public interest.”⁹ “Applicants cannot carry their burden if their

⁷ See 47 U.S.C. §§ 214(a) and 310(d).

⁸ *In re Applications of Time Warner Inc., America Online, Inc., and AOL Time Warner Inc.*, Memorandum Opinion and Order, FCC 01-12, CS Dkt No. 00-30, 2001 WL 55636, ¶ 19 (Jan. 22, 2001) (“*AOL-Time Warner Order*”) (citing *In re Applications of Ameritech Corp. and SBC Communications Inc.*, Memorandum Opinion and Order, 14 FCC Rcd. 14,712, 14,736 ¶ 46 (1999) (“*SBC-Ameritech Order*”), *rev’d in part on other grounds sub nom., Assoc. of Communications Enters. v. FCC*, 235 F.3d 662 (D.C. Cir. 2001)).

⁹ *In re Application of GTE Corp. and Bell Atlantic Corp.* Memorandum Opinion and Order, 15 FCC Rcd. 14,032, 14,046 ¶ 22 (2000) (“*GTE-Bell Atlantic Order*”) (citations omitted) (emphasis added). See also *AOL-Time Warner Order*, *supra*, ¶ 19 (citing *In re Applications of Tele-Communications, Inc. and AT&T Corp.*, Memorandum Opinion and Order, 14 FCC Rcd. 3160, 3169-70 ¶ 15 (1999) (“*AT&T-TCI Order*”)); *In re Application of WorldCom, Inc. and MCI Communications Corp.*, Memorandum Opinion and Order, 13 FCC Rcd. 18,025, 18,031 ¶ 10 n.33 (“*WorldCom-MCI Order*”) (citing 47 U.S.C. § 309(e)) (burdens of proceeding and proof rest with the applicant)).

efficiency claims are vague or speculative, and cannot be verified by reasonable means.”¹⁰

In undertaking its public interest analysis, the Commission is guided by four principal considerations:

1. Whether the transaction would result in a violation of the Communications Act or any other applicable statutory provision;
2. Whether the transaction would result in a violation of the Commission’s rules;
3. Whether the transaction would substantially frustrate or impair the Commission’s implementation or enforcement of the Communications Act and/or other related statutes, or would interfere with the objectives of the Communications Act and/or other related statutes; and
4. Whether the transaction promises to yield affirmative public interest benefits.¹¹

While there is a certain degree of overlap between the Commission’s public interest analysis and the antitrust review of the proposed merger performed by the Department of Justice, the Commission’s review process necessarily is more attuned to communications policy issues and, because of its public interest framework coupled with the allocation of the burden of proof, more rigorous.

The Commission’s analysis of public interest benefits and harms includes, but is not limited to, an analysis of the potential competitive effects of the transaction, as informed

¹⁰ *In re Applications of NYNEX Corp. and Bell Atlantic Corp.*, Memorandum Opinion and Order, 12 FCC Rcd. 19,985, 20,064 ¶ 158 (1997) (“*Bell Atlantic-NYNEX Order*”).

¹¹ *AOL-Time Warner Order*, *supra*, ¶ 20 (citing *In re Applications of MediaOne Group, Inc., and AT&T Corp.*, Memorandum Opinion and Order, 15 FCC Rcd. 9,816, 9,820-21 ¶ 9 (2000) (“*AT&T-MediaOne Order*”)); *SBC-Ameritech Order*, 14 FCC Rcd. at 14,737 ¶ 48.

by traditional antitrust principles. While an antitrust analysis, such as that undertaken by the Department of Justice . . . focuses solely on whether the effect of a proposed merger “may be substantially to lessen competition,” the Communications Act requires the Commission to make an independent public interest determination, which includes evaluating public interest benefits or harms of the merger’s likely effect on future competition. To find that a merger is in the public interest, therefore, the Commission must “be convinced that it will enhance competition.”¹²

Thus, it is incumbent upon the transfer applicants affirmatively and credibly to prove that the proposed transfer of control would enhance competition.

Moreover, transfer applicants who propose a merger to monopoly, as the transfer applicants propose here, must be held to a very high standard to prove that a such a merger – rather than some less anti-competitive means – is necessary to achieve the benefits and efficiencies they allege. Today’s Wall Street Journal reports that, for approximately 2 years, EchoStar and DIRECTV engaged in extensive discussions on ways in which they could share spectrum and achieve many of the efficiencies for which they now claim the merger is necessary.¹³ Indeed, it appears that those discussions ran right up to the point at which EchoStar decided to make its bid for DIRECTV. The article also reports that the Commission has “requested information about those earlier Hughes-EchoStar discussions and the reasons they fizzled.” The Commission is right to request a full disclosure of these matters, and the parties to this proceeding are also entitled to review this information. As we demonstrate throughout this Petition, this

¹² *AOL-Time Warner Order, supra*, ¶ 21 (citations omitted) (emphasis added).

¹³ See Andy Pasztor, “Past Meetings Could Snarl Merger of Hughes, EchoStar; FCC, Justice Department Seek Information on Once-Secret Talks and Why They Ended,” *THE WALL STREET JOURNAL*, Feb 4, 2002.

merger is not necessary to achieve many of the principal benefits the transfer applicants have alleged, and the discussions reported today may be further evidence of that fact.

II. The Transfer Applicants Have Not Met Their Burden

If consummated as proposed, this merger would completely eliminate the head-to-head competition that has characterized the DBS industry since its inception. In its place, the merger would leave a single company as the only source of multichannel video to millions of U.S. homes, and the only source of advanced digital video and broadband service to tens of millions more. New EchoStar would control:

- All of the BSS Ku-band orbital slots and spectrum assigned to the United States that allow coverage of all of the continental United States (“CONUS”);
- Through ownership or exclusive distribution relationships, 100% of the 17 million DBS video subscribers, which would make New EchoStar the nation’s largest cable or satellite company;
- Approximately one-third of the FSS Ka-band orbital slots assigned to the United States that allow CONUS coverage and that are necessary to the provision of competitive broadband services; no other U.S. licensee would hold more than 5% of U.S. CONUS Ka-band licenses;
- Both of the currently operating, and competing, platforms and technologies for the delivery of broadband access by satellite, which are and are likely to remain the only source of broadband Internet access for tens of millions of U.S. homes; and
- PanAmSat, the self-styled “world’s premier satellite services company,”¹⁴ and, by far, the largest U.S.-owned FSS operator.

This extraordinary combination of scarce resources, creating a merger to monopoly in DBS and in satellite broadband, and eliminating substantial multichannel video competition throughout the country, will produce profound harm to the public interest, as described in detail in Section III, below. EchoStar and DIRECTV face a

¹⁴ See <http://www.panamsat.com/>.

formidable challenge to show that, despite these facts and contrary to logic, the merger would actually result in increased competition and other public interest benefits. They have failed to do so.

The transfer applicants seek to paint a picture of the DBS industry as weak, hamstrung and vulnerable to being overwhelmed by cable. As shown below, the facts tell a different story. According to the FCC's recent Eighth Annual Report on competition in video programming, DBS continues to add subscribers at a growth rate of 24%, compared to 1.9% for cable,¹⁵ meaning that nearly three out of four new multichannel video subscribers are choosing DBS. DIRECTV, EchoStar and Pegasus all rank among the 10 largest multichannel providers in the United States. Moreover, both DBS platforms today offer more total channels to their subscribers than many advanced digital cable systems,¹⁶ and could continue to do so even if they provided local television service to 100 – or all 210 – DMAs. In fact, EchoStar has so much excess DBS spectrum it is using some for non-DBS commercial services.

Nevertheless, the transfer applicants claim that they need to merge in order to provide services consumers want and they cannot provide today. This argument, unsubstantiated by any reliable data, amounts to the following:

- DIRECTV and EchoStar do not currently offer services, including local-into-local, HDTV and pay-per-view, that are necessary for them to compete with digital cable

¹⁵ See *In re Annual Assessment of the Status of Competition in the Market for Delivery of Video Programming*, Eighth Annual Report, CS Dkt No. 01-129, 2002 WL 47062 ¶ 13 (rel. Jan. 14, 2002) (“*Eighth Annual Report*”).

¹⁶ See Attachment C-66.

- The only way to add these essential services is through the elimination of duplicative transmission of existing programming
- The only way to eliminate duplication in transmission is through a merger
- Satellite broadband services are characterized by significant economies of scale
- It is necessary for satellite broadband providers to realize those alleged scale economies in order to be competitive with cable broadband, and
- The merger is the *only* way to achieve these scale economies and enable “the merged company to accelerate and better promote the deployment of [satellite broadband] services to both rural and urban markets.”¹⁷

The transfer application utterly fails to quantify these supposed benefits, or to show why they could not be achieved by either of the merging firms individually, or to make any specific commitments to deliver any of the purported benefits – even to provide satellite broadband at all, much less to deploy it in a timely way, at affordable prices, to all areas of the country. The transfer applicants are deliberately vague on these points for good reason. As we show in Section IV, they do not need the spectrum the merger would allow them to control to provide these services. Similarly, the claim that the merger is necessary to support the provision of satellite broadband services is not supported by any reliable evidence nor backed by any commitment to provide advanced services. In fact, by creating a video monopoly in the areas most in need of satellite broadband service, the merger would lead to a broadband monopoly for tens of millions of Americans.

¹⁷ Application of EchoStar Communications Corp., General Motors Corp., and Hughes Electronics Corp., Consolidated Application for Authority to Transfer Control, CS Dkt No. 01-348 (filed with FCC Dec. 3, 2001) (“Application”) at 43.

III. The Merger Will Eliminate Substantial Competition And Harm The Public Interest In Multichannel Video And Broadband Markets

The proposed merger of EchoStar and DIRECTV will eliminate all competition in DBS and satellite broadband services, and will substantially reduce competition in multichannel video programming distribution (“MVPD”) throughout the United States. The result will be harm to consumers in the form of higher prices, reduced choice, degraded service and stifled innovation. These effects will be most acute in rural areas, which are served by Pegasus, where millions of consumers will be left with only one multichannel video and broadband option. The Commission, thus, cannot find that the proposed transfer is in the public interest.

A. Under Any Definition Of The Relevant Product Market, This Merger Will Substantially Lessen Competition

The Commission’s competitive analysis typically begins with a definition of the relevant product market. In this case, however, the conclusion will be the same whether the market includes the provision of only DBS, of digital MVPD services, or of all MVPD services (including both digital and analog MVPD). In each case, the elimination of direct, head-to-head competition between EchoStar and DIRECTV will cause substantial competitive harm in every geographic market throughout the United States.

One fact is clear and indisputable – this is a merger combining the only two facilities-based DBS providers in the United States. Together, EchoStar and DIRECTV control one hundred percent of the Ku-band slots capable of providing DBS coverage over the entire continental United States. Together, EchoStar and DIRECTV also control, either by outright ownership or leases, 87% of the non-CONUS DBS

frequencies.¹⁸ The proposed merger would complete the process of consolidation among DBS licensees, and result in the creation of a nationwide DBS monopoly with extraordinarily high barriers to new competitive entry.

The transfer applicants try to sidestep this issue by arguing that they compete in a broad MVPD market dominated by cable television. As discussed below, this argument ignores the many millions of consumers, especially in rural areas, who have no access to cable television and no prospect of gaining access in the future. It also ignores the tens of millions of other consumers for whom cable is a weak and declining *analog* alternative to the rich array of *digital* services offered by DBS.

The transfer applicants go to considerable lengths to minimize the degree and significance of the competition between them. But the Commission should be aware of what EchoStar has said in the recent past on that subject. Just a little over a year ago, in November 2000, EchoStar represented to the federal court hearing its antitrust case against DIRECTV that it would present evidence demonstrating the following facts:

- (a) DBS is in a separate product market from alternative sources of programming, including cable television;
- (b) A significant number of DBS subscribers view DIRECTV and EchoStar as significantly closer substitutes than alternative sources of programming, including cable television;
- (c) Cable television is an imperfect and comparatively weak substitute for DBS;
- (d) If not constrained by EchoStar, DIRECTV could raise its prices above the competitive level without experiencing a significant constraint by cable;

¹⁸ See Attachment C-99.

- (e) DBS and/or High Power DBS is superior to most cable services in several respects, including higher quality picture, substantially more programming options, and pay-per-view in a “near-on-demand” environment that consumers find more attractive than the pay-per-view environment offered by cable;
- (f) Significant numbers of consumers have subscribed to both DBS and/or High Power DBS service and cable service, reflecting that the two products are imperfect substitutes;
- (g) EchoStar is DIRECTV’s closest competitor;
- (h) Many, if not most, consumers who would switch away from EchoStar if it raised its prices relative to all other subscription programming services would turn to DIRECTV;
- (i) DIRECTV expects to profit from raising EchoStar’s costs since other potential satellite providers cannot easily enter the market and attract the customers that EchoStar is losing as a result of DIRECTV’s conduct;
- (j) There are significant entry barriers to the DBS and/or High Power DBS market;
- (k) DIRECTV and EchoStar react primarily to each other when setting equipment and service prices;
- (l) High Power DBS is the only multichannel television transmission service capable of servicing the entire continental United States;
- (m) Millions of potential DBS and/or High Power DBS customers live in areas that do not have access to cable such that, if there is no competition between DIRECTV and EchoStar, there is no competition at all;
- (n) High Power DBS is the only choice for consumers desiring a broad range of premium sports broadcasting, such as access to all professional sports league games; and
- (o) Consumers desiring as broad a range of television programming and entertainment options as possible, comprehensive premium sports coverage, maximum clarity of video and audio transmission, and ease of installation

and operation have no alternative to High Power DBS service, since cable does not offer such choices.¹⁹

EchoStar's well-articulated position in that lawsuit comports with the basic facts. It shows that, irrespective of whether there is some degree of competition between DBS and cable in some areas, cable is not a close substitute for either DBS provider. It also shows that the loss of competition between EchoStar and DIRECTV would have substantial detrimental effects on tens of millions of consumers, especially, but not exclusively, in rural areas, who will be deprived of the benefits of any competition. The transfer applicants have not shown why these facts, represented as true by EchoStar in November 2000, are no longer true.

The impact of the merger will be felt in local markets. As set forth in Dr. Rubinfeld's affidavit and report, MVPD markets are local.²⁰ A consumer in any given area can only receive cable television from the providers, if any, franchised or otherwise, in that area. Rates, service offerings, and other dimensions of competition thus vary from locality to locality. The fact that DBS providers provide service nationwide, and currently price their programming on a nationwide basis, does not affect the conclusion that the relevant markets are local. As Dr. Rubinfeld opines, regional and other non-national "promotions result in different 'effective' prices for the subscribers in particular localities, even though DBS providers may be offering nationally priced programming packages."²¹

¹⁹ Memorandum of Law in Support of Request of Rule 56 Continuance to Respond to DIRECTV Defendants' Motion for Summary Judgment at 11-13, *EchoStar v. DIRECTV*, Civ. Action No. 00-212 (D. Colo. filed Nov. 6, 2000) ("EchoStar Brief").

²⁰ See Rubinfeld Aff., ¶¶ 33-36. See also *AOL-Time Warner Order*, *supra*, ¶ 244.

²¹ See Rubinfeld Aff., ¶ 34.

B. In Rural And Other Areas Where Cable Is Not Present, EchoStar's Acquisition Of DIRECTV Is A Merger To Monopoly

By Congressional mandate, the Commission plays a unique role in preserving and developing communications services in rural America.²² In that role, the Commission consistently has focused on the impact of its decisions on rural consumers.²³ The Commission also has consistently recognized that for rural consumers, satellite services are unique and uniquely valuable.²⁴

²² See 47 U.S.C. § 151 (The Commission should make available, “so far as possible, to all people of the United States...communication service with adequate facilities at reasonable charges.”); 47 U.S.C. § 307(b) (“In considering applications for licenses...the Commission shall make such distribution of licenses...among the States and Communities as to provide a fair, efficient and equitable distribution of radio service to each of the same.”); 47 U.S.C. § 254(b)(3) (“Consumers in all regions of the nation, including low income consumers and those in rural, insular, and high cost areas, should have access to telecommunications and information services.”); *cf.* 47 U.S.C. § 1103 (authorizing the Local Television Loan Guarantee Board to provide loan guarantees for projects delivering local television signals to nonserved and underserved areas).

²³ See, e.g., *In re Flexibility for Delivery of Communications by Mobile Satellite Service Providers in the 2 GHz Band, the L-Band, and the 1.6/2.4 GHz Band*, Notice of Proposed Rulemaking, 16 FCC Rcd. 15,532, 15,543 ¶ 23 (2001) (proposing new services to promote the provision of broadband communications services to rural areas); *In re Extending Wireless Telecommunications to Tribal Lands*, Report and Order, 15 FCC Rcd. 11,794, 11,799-800 ¶ 14 (2000) (adopting initiatives to promote the deployment of wireless telecommunications services to tribal lands); *In re Amendment of the Commission’s Rules to Establish New Personal Communications Services, Narrowband PCS*, Second Report and Order and Further Notice of Proposed Rulemaking, 15 FCC Rcd. 10,456, 10,469 ¶ 24 (2000) (setting coverage requirements so as to improve service to rural areas); *In re 1998 Biennial Regulatory Review Spectrum Allocation Limits for Wireless Telecommunications Carriers*, Report and Order, 15 FCC Rcd. 9,219, 9,222 ¶ 2 (1999) (setting spectrum caps so as to improve service to rural areas); *In re Applications of RKO General Inc.*, 4 FCC Rcd 4,997, 4,998 ¶ 7 (1989) (allocating broadcast licenses so as to improve service in underserved areas).

²⁴ See *In re Inquiry into the Development of Regulatory Policy in Regard to Direct Broadcast Satellites*, Report and Order, 90 FCC2d 676, 680 ¶ 13 (1982) (creating DBS service because it “holds unique promise of meeting the programming needs of remote, underserved households”); *In re Flexibility for Delivery of Communications by Mobile Satellite Service Providers in the 2 GHz Band, the L-Band, and the 1.6/2.4. GHz Band*, Notice of Proposed Rulemaking, 16 FCC Rcd. 15,532, 15,543 ¶ 23 (2001) (“MSS systems continue to offer the potential to achieve this goal [of providing service to rural areas.]”); *In re Establishment of Policies and Service Rules for the Mobile Satellite Service in the 2 GHz Band*, Report and Order, 15 FCC Rcd. 16,127, 16,144-46 ¶¶ 34-35 (2000) (“[We] believe satellites are an excellent technology for delivering basic and advanced telecommunications services to unserved, rural, insular, or economically

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In the many rural areas where cable television is not available, the proposed merger eliminates all competition. EchoStar made this point succinctly in its antitrust suit against DIRECTV: “Millions of potential DBS and/or Higher Power DBS customers live in areas that do not have access to cable such that, if there is no competition between DIRECTV and EchoStar, there is no competition at all.”²⁵ In those areas, whether the product market is defined as MVPD or DBS, creating a DBS monopoly through this merger will deprive millions of consumers – largely, rural Americans – of a choice in multichannel video service.

The transfer applicants have tried to minimize this concern by significantly understating the percentage of homes without access to cable.²⁶ A report by the Rural Utilities Service of the Department of Agriculture and the NTIA has shown that the percentage of homes without cable access could be as high as 19%.²⁷ And, if one looks

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isolated areasWe remain committed to encouraging the expeditious delivery of telecommunications services, via satellite services, to unserved communities.”); *Extending Wireless Telecommunications to Tribal Lands*, 15 FCC Rcd 11,794, 11,799 ¶ 13 (2000) (“Satellites also provide communications opportunities for communities in geographically isolated areas, such as mountainous regions and deep valleys, where rugged impassable terrain may make service via wireless or wireline telephony economically impractical.”); *In re Establishment of Rules and Policies for the Digital Audio Radio Satellite Service in the 2310-2360 MHz Frequency Band*, Report and Order, Memorandum Opinion and Order, and Further Notice of Proposed Rulemaking, 12 FCC Rcd. 5,754, 5,756, ¶ 1 (1997) (“Satellite DARS has the technological potential to serve listeners in areas of the country that have been underserved.”); *Establishing Rules and Policies for the Use of Spectrum for Mobile Satellite Service in the Upper and Lower L-band*, Notice of Proposed Rulemaking, 11 FCC Rcd. 11,675 11,680 ¶ 12 (1996) (“MSS can serve areas of the country that are too remote or sparsely populated to be served by terrestrial land mobile systems.”).

²⁵ See EchoStar Brief, *supra*, at 12.

²⁶ See Application at 39-40.

²⁷ See National Telecommunications and Information Administration (NTIA) & Rural Utilities Service (United States Department of Agriculture), *Advanced Telecommunications in Rural America: The Challenge of Bringing Broadband Service to All Americans*, at 19 & n.62 (Apr. 2000) (“NTIA/RUS Report”). See also *In re Annual*

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at the number of U.S. Housing Units according to the 2000 Census and the number of homes passed by cable from the “2001 Warren Cable Factbook,” as many as 24 million homes nationwide would face an MVPD monopoly if the merger were approved.²⁸ Rural consumers would be disproportionately affected. Attachments C-4 to C-55 provides a breakdown of cable TV penetration for each state and by county within each state. In many counties, cable access is significantly less than 20%.

There is a range of estimates and some controversy over the number of U.S. homes that lack access to cable.²⁹ Pegasus believes that the actual number of unserved homes throughout the country is closer to the 24 million estimate, and that the number of unserved homes in rural areas is disproportionately high, since both DIRECTV and

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Assessment of the Status of Competition in the Market for the Delivery of Video Programming, Seventh Annual Report, 16 FCC Rcd. 6,005, 6,016, ¶ 18 (Jan. 8, 2001) (“*Seventh Annual Report*”) (recognizing that some estimates of cable access are as low as 81%).

²⁸ According to the 2000 Census, the number of U.S. Housing Units was 115,904,641. See U.S. Census 2000, available at <http://www.census.gov/main/www.cen2000.html>. The Warren Cable Factbook listed 91,814,665 homes as passed by cable as of October 1, 1998. 67 Television and Cable Factbook J-98 (Albert Warren ed., Warren Pub. Inc.) (“1999 Warren Cable Factbook”).

²⁹ There are many flaws in any system that attempts to measure homes passed by cable. See NTIA/RUS Report at 19 (noting that cable operators have no easy way of determining what type of households they do not serve). Homes passed are merely estimates by cable companies of the number of housing units their plant passes. For older or smaller cable systems that do not have “as built” maps showing the location of housing units on each street passed, estimates of homes passed are little more than guesses. In any event, there is no effective way for a cable system to know whether a “home passed” is a “housing unit” or a “household” unless the home is a cable subscriber. Nor is there any way of knowing whether the home is occupied year-round. Pegasus believes it is most reasonable to estimate the percentage of homes passed by cable by dividing reported cable homes passed into total housing units. A more accurate estimate would be made as follows: (i) subtract cable homes passed from U.S. housing units; (ii) derive the ratio of U.S. households *plus* seasonal households to U.S. housing units – this will determine the percentage of U.S. housing units that are *potential* subscribers to multichannel video; and (iii) multiply the ratio derived in (ii) by the total derived in (i) to determine the number of U.S. households *not* passed by cable.

Pegasus have reported that approximately 30% of their customers have no access to cable. In any event, it cannot be disputed that the number of U.S. homes for which this will be a merger to monopoly is very substantial. These consumers will not longer have *any* choice in multichannel service if this merger is consummated.

**C. In Many Rural Areas With Access To Analog Cable
Only, There Will Be No Effective Competition to DBS**

Even in many areas with cable television, cable is not and will not be an effective constraint on a DBS monopoly. Consumers in many rural markets are served by antiquated analog cable systems. These systems offer few of the services, capabilities, and technological advances of DBS. As illustrated by the following chart, where DBS offers over 200 channels with digital quality picture and sound, rural analog cable offers significantly fewer channels – almost 35% of cable subscribers have access to 53 or fewer analog cable channels.³⁰

³⁰ See Attachment C-66 (table showing the channel capacity of existing cable systems as of Dec. 2000).

Channel Capacity of Existing Cable Systems as of December 2000³¹

Channel Capacity	# Systems	% Total Systems	Subscribers	% Total Subs
125 +	13	0.13%	858,586	0.30%
91-124	90	0.88%	2,978,321	4.30%
54-90	2,190	21.38%	37,814,695	57.52%
30-53	5,716	55.80%	17,798,869	33.30%
20-29	735	7.18%	392,919	1.12%
13-19	218	2.13%	41,909	0.11%
6-12	247	2.41%	56,622	0.12%
5 only	7	0.07%	833	0.00%
under 5	5	0.05%	3,749	0.01%
not avail.	1,022	9.98%	4,973,851	2.23%
TOTALS	10,243		64,920,534	

The economics of rural cable suggest that it will be a diminishing factor in the future. Analysts predict that many rural analog cable systems will go dark within the next few years. For example, a Credit Suisse First Boston (“CSFB”) report estimates that approximately 8,720 cable systems serving 8.2 million subscribers in rural territories could become extinct over the next five years as their product becomes less and less competitive. CSFB predicts that the typical small cable operator will not be able to generate enough cash to cover basic operating and maintenance requirements once its subscriber penetration falls to 30% or below.³²

Most analog cable systems in rural areas cannot afford to upgrade to digital to match DBS. Indeed, cable systems with less than 5,000 subscribers – consisting of some 7,748 systems nationwide with nearly 7 million subscribers³³ – have no economic path to

³¹ 69 Television and Cable Factbook F-2 (Albert Warren, ed., Warren Pub. Inc.) (“2000 Warren Cable Factbook”).

³² Credit Suisse First Boston, *Natural Selection: DBS Should Thrive as the Fittest to Serve Rural America* at 4, Oct. 12, 2001 (“CSFB Report”).

³³ See 2001 Warren Cable Factbook.

digital upgrade. Advanced digital cable systems require a 750 MHz cable plant. Achieving this entails upgrade costs between \$10,000 and \$15,000 per mile. Because rural home density averages 11 homes per square mile,³⁴ it would rarely be economical for such a cable system to upgrade. The CSFB report states: “Low household density and small system sizes create business model inefficiencies that will likely prevent most small cable operators, concentrated primarily in C and D counties (i.e., rural America), from providing digital cable and cable modem services.”³⁵

The demise of rural cable is already underway. Classic Communications, focused on rural areas, grew into the 10th largest cable company in the U.S. by 1998. In 2001, Classic filed for bankruptcy with a per subscriber debt of \$1,448. Despite a market penetration of 54%, Classic could not support the growth necessary to sustain a rural cable system.³⁶ Similarly, Interstate Cable ceased operations in late January 2002, leaving several hundred customers in four rural Oregon communities without cable service.³⁷ Commenting on the situation, one Oregon cable operator observed, “This isn’t so surprising. You’ll probably see a lot more fallout with operators of extremely small systems that couldn’t compete.”³⁸

³⁴ The figure for rural home density is based on AC Nielsen & Co. statistics for C & D (rural) counties.

³⁵ See CSFB Report at 4.

³⁶ See *id.*

³⁷ See Linda Haugsted, *Faltering Oregon Operator Goes Dark*, MULTICHANNEL NEWS, Jan. 28, 2002, available at <http://www.tvinsite.com/multichannelnews/login.asp?returnURL=http://www.tvinsite.com/multichannelnews/index%2Easp%3Flayout%3Dstory%26articleId%3DCA192894%26pubdate%3D01%2F28%2F2002%26stt%3D001%26display%3DsearchResults®opt=invite>.

³⁸ *Id.* (quoting Neal Schnog, President of Univision LLC, a small cable operator with approximately 21,000 subscribers in Oregon).

Thus, many rural consumers who today have a choice between digital DBS services and analog cable will face the same monopoly threat as those without any cable access. If this merger is approved, the only multichannel video choice they may have is a DBS monopolist, New EchoStar.³⁹

D. Even In Areas With Access To Full-Featured Cable, Consumers Will Be Harmed By The Proposed Transaction

Even in the areas where consumers have access to digital cable or sophisticated analog systems, the loss of competition between EchoStar and DIRECTV will harm competition and consumers. As the Commission has recognized,⁴⁰ and as the Merger Guidelines explain,⁴¹ horizontal mergers such as this one can produce two types of anti-competitive effects – unilateral effects and coordinated effects. Both will result from this merger.

1. Because EchoStar And DIRECTV Are The Two Closest Substitutes For One Another, The Merger Creates A Strong Likelihood Of Unilateral Anti-Competitive Effects

The nature and structure of DBS competition make it likely that unilateral anti-competitive effects will result from this merger. Unilateral effects arise when a merger

³⁹ Nor will other MVPD technologies, such as C-band, protect consumers from a DBS monopoly in areas where meaningful cable competition is not available. While C-band home satellite gained acceptance in rural areas prior to the introduction of DBS, it increasingly has been eclipsed by DBS. According to the Eighth Annual Competition Report, C-band subscribership fell by some 23% last year to just about 1 million subscribers. *Eighth Annual Report, supra*, ¶ 67. The much larger up-front consumer investment required by C-band, the very large dish size and the lack of much attractive programming and advanced features and services has led to this steady decline. Nor will other potential technologies, such as Ka-band satellite, MMDS, LMDS, or MVDDS compete significantly with DBS in rural and other uncabled areas in the near future. *See Rusch Aff.*, ¶¶ 50-54.

⁴⁰ *See, e.g., GTE/Bell Atlantic Order, supra*, at 14,104 ¶ 142 n.334.

⁴¹ DEPT. OF JUSTICE AND FEDERAL TRADE COMM’N HORIZONTAL MERGER GUIDELINES §§ 0.1, 2.1, and 2.2 (1992) (“Guidelines”).

enables a firm to increase price or otherwise compete less aggressively independently of how rivals behave. Such effects can occur where the products of the merging firms are sufficiently similar that there is considerable rivalry between them and they are closer substitutes for one another than are other products.⁴² Because EchoStar and DIRECTV are closer substitutes for one another than cable is for either, the proposed merger raises the substantial likelihood of unilateral anti-competitive effects.

There is substantial evidence that EchoStar and DIRECTV compete very closely with each other and that competition with cable is more attenuated. Indeed, in its antitrust suit against DIRECTV, EchoStar asserted that head-to-head competition between DBS providers is more direct and has greater impact than competition from cable: “DIRECTV and EchoStar react primarily to each other when setting service and equipment prices.”⁴³

Examining the competitive behavior of EchoStar and DIRECTV shows clearly that they compete vigorously with one another:

- *Pricing*: EchoStar and DIRECTV prices for comparable basic programming packages are within \$1 of each other. This can hardly be coincidental. Cable rates, meanwhile, vary widely from market to market.

⁴² *In re Applications of NYNEX Corp. and Bell Atlantic Corp.*, Memorandum Opinion and Order, 12 FCC Rcd. 19, 985, 20,038-39, ¶ 102 (1997) (“With respect to merging firms, a merger may lead to particularly strong increases in the acquiring firm’s ability to affect market performance unilaterally where the merging firms’ services are very close substitutes for each other.”) (“*Bell Atlantic-NYNEX Order*”).

⁴³ EchoStar Brief, *supra*, at 12. Paradoxically, Dr. Willig says he was told by executives of *both* EchoStar and DIRECTV that the pricing of the other DBS provider “plays little (if any) role in their own pricing decisions.” Willig Aff., ¶ 6 n.5. As noted below, the objective evidence indicates that there is a strong reaction of each firm to the other’s pricing, and that EchoStar’s November 2000 statement was the correct one.

Level of Service	DISH SERVICE	DISH PRICE	DIRECTV SERVICE	DIRECTV PRICE
Low	America's Top 50	\$ 22.99	Select Choice	\$ 21.99
Medium	America's Top 100	\$ 31.99	Total Choice	\$ 31.99

- *Pricing Trends:* The similarity in pricing is not a recent phenomenon, but has persisted over time. Historically, EchoStar and DIRECTV pricing has been remarkably similar. From 1996 through 2000, DBS prices remained the same, while cable rates rose an average of 7% per year.⁴⁴ In fact, through the third quarter of 2001, the DBS competitors instituted only one price increase. During the same time period, cable rates rose an average of 7% per year.

	Year Over Year Percent Price Increase					Average
	1996	1997	1998	1999	2000	
Cable *	9%	9%	10%	5%	3%	7%
DBS **	0%	0%	0%	0%	3%	0.6%

- *Equipment Pricing:* DBS systems were priced at \$800-1000 when DIRECTV was the only DBS provider in 1994-95. When EchoStar entered the market in 1996, equipment prices fell to \$400-600.⁴⁵ Now, 2 receivers (and a dish) can be obtained for \$50 or less. This is the result of direct competition between the DBS providers.
- *Packages:* EchoStar and DIRECTV offer remarkably similar programming packages. EchoStar's "America's Top 100" has many of the same channels as DIRECTV's "Total Choice" package. New premium packages, such as America's Everything and Total Choice Platinum, also offer many of the same channels.

⁴⁴ Cable data derived from the FCC Report on Cable Prices – February 2001, *In re Implementation of Section 3 of the Cable Television Consumer Protection and Competition Act of 1992*, Report on Cable Industry Prices, 16 FCC Rcd. 4,346 (2001), and the Fifth Annual Assessment of the Status of Competition in Markets for Delivery of Video Programming, *In re Annual Assessment of the Status of Competition in Markets for the Delivery of Video Programming*, Fifth Annual Report, 14 Comm. Reg. (P&F) 923, 1998 WL 892964 (1998). DBS data derived from internal Pegasus data regarding pricing.

⁴⁵ A 1997 Wall Street Journal article reported that EchoStar CEO Ergen "dropped the price of his 18-inch satellite dish to \$200 from \$600, forcing competitors to follow." See Mark Robichaux, *Who's News: EchoStar Chief Must Build Link to Murdoch*, WALL ST. J., Feb. 26, 1997, available at 1997 WL-WSJ 2410829.

- *Programming:* EchoStar often promotes its program offerings by comparisons to DIRECTV. An August 2001 letter to DISH retailers noted that “As of right now, the World Wrestling Federation is not making their next show ‘Unforgiven’ available to DIRECTV! This allows a great opportunity for you to convert some of your DIRECTV customers to DISH Network.”⁴⁶ Similarly, DIRECTV’s “Para Todos” marketing materials provide a side-by-side channel comparison between Para Todos and DISH’s Latino packaging, while only citing the total number of Hispanic-oriented channels offered by cable companies.⁴⁷ To combat DIRECTV’s exclusive contract with the NFL for “NFL Sunday Ticket,” EchoStar offered customers “Fox Sports Net” which purportedly offers more than 2000 hours of sports programming per month from 20 Fox Sports Net affiliates.⁴⁸
- *Promotions:* EchoStar and DIRECTV tend to focus on each other in promotions. For example, a 2001 EchoStar advertisement refers to DISH as “The Only Satellite TV System You Get Free with Free Installation” without mention of cable.⁴⁹ Another EchoStar advertisement invited consumers to compare DISH’s per channel cost first to DIRECTV, then to Primestar, then to USSB, and finally to “compare your local cable bill.”⁵⁰
- *Bounty Programs:* EchoStar has initiated a number of “bounty programs” aimed at retailers to entice them to switch customers from DIRECTV to DISH. In a 1998 “Direct to Home Bounty Program,” EchoStar promised retailers \$100 for “each new primary activation acquired from DIRECTV, Primestar or C-band.”⁵¹ The program specified that no cable bills would be accepted as proof as switching a competitor’s customer to DISH.⁵² A 2001 EchoStar bounty program was aimed only at DIRECTV. The “TRADE UP TO DISH Promotion” enabled retailers to offer DIRECTV customers half-priced DISH PVR receiving equipment and a monthly credit of \$21.99 on their DISH bills.⁵³ EchoStar and DIRECTV participated in a fierce battle in 1998-1999 to obtain former Primestar Satellite customers with both companies initiating numerous bounty programs.⁵⁴
- *Innovation:* DIRECTV and EchoStar compete vigorously to introduce advanced services and new technology. For example, the companies battled to be

⁴⁶ See Attachment C-70.

⁴⁷ See Attachment C-84.

⁴⁸ See Attachment C-88 to C-89.

⁴⁹ See Attachment C-90.

⁵⁰ See Attachment C-91.

⁵¹ See Attachment C-92.

⁵² See *id.*

⁵³ See Attachment C-94 to C-95.

⁵⁴ See, e.g., Attachment C-96.

the first to introduce personal video recording and interactivity.⁵⁵ Likewise, both companies spend large sums to improve satellites, set-top boxes, receiving dishes, and other innovations.⁵⁶ Cable has had no impact on the pace and direction of these innovations.

- *Dealer and Distribution Networks:* DIRECTV and EchoStar compete to establish comprehensive dealer and distribution networks. This fierce competition results in subsidies and special incentives to dealers, which may, in turn, lower the effective price of DBS equipment to the consumer. This competition will disappear following the merger.

Consumers in every type of market – rural to urban – have benefited from the head-to-head competition between EchoStar and DIRECTV. For example, as described earlier, EchoStar’s entrance into the DBS market significantly brought down equipment prices. When DIRECTV was the only DBS provider, equipment and installation costs were well above what many consumers could afford – up to \$1000. Initially, DIRECTV chose to license only one manufacturer to make the set-top receiving equipment. Then, EchoStar entered the market with a vertically integrated strategy that allowed it to internally manufacture set-top boxes and focused on charging lower up-front equipment

⁵⁵ See, e.g., Monica Hogan, *DBS Eyes Record Sales in 2000*, MULTICHANNEL NEWS, Vol. 21, No. 1, at 1, Jan. 3, 2000 (reporting that “EchoStar last month added personal-video-recording features to its DishPlayer system, which already included WebTV’s Internet-over-television service . . . [and that] DirecTV plans to show its first AOL [America Online Inc.] TV boxes at the CES this week, along with DBS receivers with built-in TiVo Inc. personal video recorders”).

⁵⁶ See EchoStar Communications Corp., Form 10-K for Fiscal Year Ended Dec. 31, 2000, at 63 (filed with Securities & Exchange Comm’n Mar. 31, 2001; file no. 0-26176) (“EchoStar Form 10-K”) (reporting that “[r]esearch and development costs totaled \$8 million, \$10 million and \$17 million for the years ended December 31, 1998, 1999, and 2000, respectively”); Hughes Electronics Corp., Form 10-K for Fiscal Year Ended Dec. 31, 2000, at 39 (filed with Securities & Exchange Comm’n Mar. 6, 2001, file no. 0-26035) (“Hughes Form 10-K”) (reporting that “[e]xpenditures for research and development were \$129.3 million in 2000, \$98.8 million in 1999 and \$92.6 million in 1998”).

prices to consumers. Once EchoStar began offering equipment in the \$200 range, DIRECTV was forced to follow suit.⁵⁷

Today, competition between EchoStar and DIRECTV on equipment pricing remains intense and has provided great benefits to consumers. The cost to consumers for satellite dishes and receivers has dropped to as low as \$50 or less, in large part because the DBS providers subsidize the equipment and installation costs. The merger will eliminate this competition completely. Just as competition from cable did not have the impact on equipment pricing that the entry of a new DBS provider did, it will not constrain the equipment pricing of a DBS monopolist.

The two DBS platforms also have competed vigorously to enhance their video offerings through the introduction of new satellite-based services and innovation. EchoStar stated in its most recent SEC Form 10-K that the company is continuing to expand its offerings to include new interactive, Internet, and high-speed data services.⁵⁸ In 2000 and 2001, EchoStar made “strategic investments” in StarBand Communications to offer consumers two-way, high-speed satellite Internet access along with DISH Network television programming via a single dish.⁵⁹ Moreover, in March 2000, EchoStar invested \$50 million in Wildblue Communications, a company that plans to offer high-speed data services in 2003, and the two companies plan to develop jointly a single

⁵⁷ See Mark Robichaux, *Who’s News: EchoStar Chief Must Build Link to Murdoch*, WALL ST. J., Feb. 26, 1997, available at 1997 WL-WSJ 2410829.

⁵⁸ See EchoStar Form 10-K, *supra*, at 2.

⁵⁹ See *id.*; EchoStar Communications Corp. Form 10-Q for Quarterly Period Ended Sept. 30, 2001, at 5 (filed with U.S. Securities & Exchange Comm’n; file no. 0-26176) (“EchoStar Form 10-Q”).

receiver for video and Internet access functions.⁶⁰ EchoStar also has expended considerable capital on acquiring sophisticated digital broadcast operations centers, on developing spot beam technologies to offer more local channels, and on developing receiver systems in connection with its subscriber packages.⁶¹ Hughes' most recent SEC filings reveal similar innovations. For example, in 2000, Hughes added two-way capabilities to its nationwide high-speed satellite Internet service, DirecPC.⁶² Moreover, Hughes touted the construction and expected launch of a high-power spot-beam satellite that would "provide additional capacity for new local channel service or other new services."⁶³

As noted below, the merger will eliminate satellite broadband competition. But even within the context of their video offerings, the merger will end the competition to innovate and offer consumers the most technologically advanced and efficient service.

The transfer applicants have contended that the merger will promote the provision of local-into-local service, *i.e.*, the transmission of local broadcast signals into local markets. We show below that the merger is unnecessary to provide increased transmission of local signals. Indeed, competition between EchoStar and DIRECTV has been a key factor stimulating the rollout of local service to date.

⁶⁰ See EchoStar Form 10-K, *supra*, at 2..

⁶¹ See *id.* at 3, 4; EchoStar Form 10-Q, *supra*, at 17, 25.

⁶² See Hughes Form 10-K, *supra*, at 1.

⁶³ *Id.* See also Hughes Electronic Corp., Form 10-Q for Quarterly Period Ended Sept. 30, 2001, at 18 (filed with U.S. Securities & Exchange Comm'n; file no. 0-26035) ("Hughes Form 10-Q").

Before 1999, DIRECTV did not support EchoStar's efforts to gain passage of legislation that would allow delivery of local broadcast signals to local markets, instead encouraging consumers to solve the local signal issue by using antennas in conjunction with their satellite dishes.⁶⁴ DIRECTV's reticence toward a local-into-local strategy related to its view that EchoStar's local-signal strategy made little "economic sense."⁶⁵ However, in April 1999, as EchoStar unveiled an aggressive plan to launch new satellites and expand local channel capacity, DIRECTV was reported to appear "to be warming up to the idea of providing local channels."⁶⁶ In fact, by May 1999, in "a big strategic shift," DIRECTV announced plans to offer local signals to approximately twenty local markets, stating that "we wouldn't be doing this if we didn't think it was going to expand the popularity of DIRECTV."⁶⁷ The timing of local roll-outs into particular markets since then illustrates the degree to which EchoStar and DIRECTV compete to offer service.⁶⁸ Eighty-five percent of the top 20 markets were covered by both competitors within 30 days of one another. Thus, it is evident that competition between the two largest DBS providers was the main impetus behind DIRECTV's change in business plans and the eventual roll-out of local-into-local service.

⁶⁴ See *DBS Execs Engage in Rhetorical Battle at New York Satellite Conference*, COMMUNICATIONS TODAY, Sept. 17, 1997, available at 1997 WL 13696432; Jim McConville, *DBS Bugged Down on Local Signal Issue*, ELECTRONIC MEDIA, Sept. 22, 1997, available at 1997 WL 8290274.

⁶⁵ See *Ergen Alone in Calling Local Signals Essential to DBS*, 4 MEDIA DAILY No. 5, Apr. 29, 1998, available at 1999 WL 9943155.

⁶⁶ See *EchoStar Plans Launch of Spot Beam Birds to Offer Local Signals*, 22 SATELLITE NEWS No. 15, Apr. 12, 1999, available at 1999 WL 6684365.

⁶⁷ See Alan Breznick, *DIRECTV to Offer Local Broadcast Signals by Year's End*, CABLE WORLD, May 10, 1999.

⁶⁸ See Attachment C-64 to C-65 for a timeline of both companies' local market expansion.

The transfer applicants now claim that their merger will enable them to deliver local service to more markets because they will have more spectrum. As shown below, it is a lack of will – not a lack of spectrum – that has inhibited the delivery of local-into-local service since the enactment of the Satellite Home Viewer Improvement Act of 1999 (“SHVIA”).⁶⁹

2. A Merger To Duopoly Also Would Harm MVPD Consumers Nationwide

Viewed even in the light most favorable to the transfer applicants, by creating a single provider of DBS (and satellite broadband) service, the merger would create a nationwide MVPD duopoly. In each local market, customers would be able to choose only between New EchoStar and the local cable company. As the Court of Appeals for the District of Columbia Circuit recently noted, a duopoly in an industry characterized by high barriers to entry – which certainly describes the MVPD market – is what the antitrust laws have sought to prevent.⁷⁰ As with any duopoly, tacit and/or explicit coordinated interaction will be facilitated with only two providers.⁷¹ Each competitor – the lone cable system and the sole DBS provider – will have greater freedom to raise

⁶⁹ Pub. Law No. 106-113, 113 Stat. 1501, 1501A-526 to 1501A-545 (1999). Shortly after SHVIA was passed, both EchoStar and DIRECTV initiated litigation to overturn that law. Perhaps, in an effort not to compromise their litigation position, both have been slow to add as many local markets as they could.

⁷⁰ See, e.g., *Federal Trade Comm’n v. H.J. Heinz Co.*, 246 F.3d 708, 715 (D.C. Cir. 2001) (“[There have been] no significant entries in the baby food market in decades and ... new entry [is] difficult and improbable. . . . As far as we can determine, no court has ever approved a merger to duopoly under similar circumstances.”).

⁷¹ See Guidelines, *supra*, § 2.12.

prices and less pressure to offer promotions, new programming packages, and technical innovations.⁷²

E. The Merger Will Eliminate Satellite Broadband Competition

This merger will eliminate current choices in satellite broadband, and significantly reduce the overall broadband choices that will be available to rural consumers. The Commission, in its AOL/Time Warner and AT&T/MediaOne Orders,⁷³ recognized the importance of maintaining competition in the emerging broadband market. The combination of Hughes and EchoStar raises troubling issues in this market and does not create any efficiencies that have the potential of benefiting consumers.

Even more dramatically than video services, DSL and cable modem high speed Internet services have been slow to reach rural areas. Hughes has stated that “1/3 of all the homes in America, 30-40 million, will never be covered by DSL or cable.”⁷⁴ The

⁷² The transfer applicants’ economist, Dr. Willig, asserts that coordination would be difficult because cable prices differ from market to market and, thus, New EchoStar would have trouble figuring out how to coordinate. *See Willig Aff.*, ¶ 29. He then turns around and claims that a uniform national price by New EchoStar would be constrained by cable, which necessarily requires that the DBS provider respond in a unitary way to the behavior of cable operators. *Id.* ¶ 38-39. The task of coordination may be simplified by accelerating consolidation among cable operators, as exemplified by the proposed merger of AT&T Broadband and Comcast. In any event, coordination need not take the form of specific price-matching on monthly fees. Instead, it can be manifested by general increases in price levels, elimination of promotional offers and a variety of other techniques.

⁷³ *See AOL-Time Warner Order, supra*, at 6,552 ¶ 12 (2001) (imposing conditions on the merged entity to serve the policies of the Communications Act, including a “preference for competitive telecommunications markets, the existence of diverse platforms and providers, the promotion of innovation, and rapid deployment of advanced telecommunications services”); *AT&T-MediaOne Order, supra*, at 9,871 ¶ 123 (approving merger because compliance with terms of DOJ’s proposed consent decree sufficiently protected competition in the nascent broadband market and promising to monitor the provision of broadband services to ensure that competition grows as expected).

⁷⁴ Attachment C-3.

number of central offices enabled for DSL in rural areas is miniscule.⁷⁵ An NTCA survey underscored the difficulties of bringing wired broadband to rural areas and concluded that “[u]nder current conditions, customers in the most remote locations will not be able to access broadband” within the next few years.⁷⁶ The NTIA/RUS report likewise found that “the cost to serve a customer increases the greater the distance among customers.”⁷⁷ Given the difficulties of bringing wired broadband technology to rural areas, it is clear that satellite broadband will be the primary means of erasing the urban/rural digital divide and bringing high speed Internet access to rural areas.

With respect to broadband services, the transfer applicants claim that they need to consolidate in order to go forward with deployment of Ka-band satellites.⁷⁸ This claim, however, is inconsistent with the statements that they have been making to the Commission for several years now – including very recently – that they are each, separately, committed to deployment of broadband satellite systems and have been building separate Ka-band satellites for several years.

Hughes publicly has stated its commitment of \$1.4 billion to its Spaceway Ka-band system.⁷⁹ According to statements it made to the Commission just last month, it has three Ka-band satellites under construction and expects to launch its first Ka-band

⁷⁵ See Attachment C-2.

⁷⁶ National Telephone Cooperative Association, *NTCA 2001 Internet/Broadband Availability Survey Report* 10 (Dec. 2001) (citing long loops, deployment costs, and low demand among the reasons wired broadband would be slow to reach additional rural customers).

⁷⁷ NTIA/RUS Report, *supra*, at ii.

⁷⁸ See Application at 43-49.

⁷⁹ See Press Release, Hughes Electronics Corp., *Hughes to Invest \$1.4 Billion in Spaceway Broadband Satellite System*, Mar. 17, 1999.

satellite in the first half of 2003.⁸⁰ Hughes and its affiliates have ample access to Ka-band orbital resources to implement a broadband satellite business. Together with its PanAmSat subsidiary, Hughes has Commission licenses for 25 Ka-band orbital locations, including what may be the three best full-CONUS orbital assignments, at 99°WL, 101°WL, and 103°WL.

While the transfer application asserts that EchoStar has undertaken only a “cautiously modest [Ka] project, equipped with only a limited number of spot beams designed to serve only a few geographical areas in the United States,”⁸¹ that is different than what EchoStar previously has represented. For example, EchoStar has told the Commission that it is building two Ka-band satellites, one of which (the satellite licensed to operate at 113°WL) it has told the Commission it is prepared to launch and begin using to provide service in just four months, by May 2002.⁸² EchoStar also told the Commission, in requesting approval for the transfer of control of Visionstar’s license for 113°WL, that the satellite was under construction and would be launched on time.⁸³ The Commission accepted this representation and, in granting the application, imposed an affirmative obligation on EchoStar to tell the Commission if it will not meet the

⁸⁰ See Letter to Magalie Roman Salas, Secretary, FCC, from John P. Janka, Hughes Electronics Corp., at 16 (Jan. 14, 2002) (for files SAT-MOD-20011221-00135 through 00136).

⁸¹ Application at 46.

⁸² See EchoStar Satellite Corp., Annual Report to FCC (Jul. 19, 2001).

⁸³ See Letter to Thomas S. Tycz, Chief, Satellite and Radiocommunications Division, International Bureau, FCC, from Michael R. Gardner, Counsel, VisionStar, Inc., and Pantelis Michalopoulos, Counsel, EchoStar VisionStar Corp., at 4 (June 7, 2001) (“Since December 2000, Lockheed has completed substantial work on construction of VisionStar’s satellite.”).

May 2002 milestone.⁸⁴ Pegasus is not aware that EchoStar has ever informed the Commission that it will be unable to meet its May 2002 milestone.

With respect to its satellites at 121°WL and 83°WL, EchoStar stated affirmatively in its 2001 Annual Status Report that it “has already entered into a binding contract for its Ka-band satellite at 121° W.L. and is proceeding with construction of that satellite, significantly ahead of its milestones.”⁸⁵ In addition to the orbital assignments at 113°WL, 121°WL, and 83°WL, Echostar has a substantial minority interest⁸⁶ in WildBlue, which reportedly also will launch a Ka-band satellite system in 2002.⁸⁷

Not only do the transfer applicants have substantial Ka-band spectrum and facilities for their broadband operations, but both currently are operating competing satellite broadband businesses – for Hughes, DIRECPC and DIRECWAY, and for EchoStar, StarBand. There is little question that both parties had every intention to invest in their broadband offerings and continue to expand their respective services. A recent Hughes press release touts the success of DIRECWAY, and indicates that the company remained committed to developing broadband.⁸⁸ Hughes expects DIRECWAY subscribership to increase from 100,000 to between 200,000 and 300,000 this year

⁸⁴ See *In re Application of VisionStar, Inc., Shant Hovnanian, and EchoStar VisionStar Corp.*, DA 01-2481, 2001 WL 1327105 ¶ 23 (Oct. 23, 2001).

⁸⁵ See EchoStar Satellite Corp., Annual Report to FCC (July 19, 2001).

⁸⁶ See Application, Attachment D, at 2.

⁸⁷ See WB Holdings 1 LLC, Annual Report to FCC, at 2 (June 30, 2001) (“Wildblue has . . . begun construction on its first satellite which is currently on schedule for launch in the first half of 2002.”).

⁸⁸ *DirecWay Tops 100,000 Subscribers*, 25 SATELLITE NEWS No. 2, Jan. 14, 2002, available at 2002 WL 8254866 (citing Hughes CEO Pradman Kaul as expressing optimism about the continued success of DIRECWAY and the potential for growth).

alone.⁸⁹ Even the transfer application does not suggest that the parties would not continue to innovate and provide satellite broadband offerings through the Ka-band. Clearly, without the merger, the parties would continue to innovate and provide satellite broadband services utilizing their Ka-band authorizations.

Moreover, the only companies poised to bring satellite broadband to rural areas are those currently providing satellite video services. The reason for this is simple – as the transfer applicants make clear, “consumers increasingly demand” a bundled package of video and broadband.⁹⁰ MSOs have the ability to bundle cable video services with high speed Internet services. The inability of other firms to offer satellite video services would inhibit new broadband entry.

There are significant cost savings associated with providing a consumer with both video and broadband service. A DBS provider can use much of its existing business operations and infrastructure, as well as the crucial distribution channels, to support a broadband offering. A DBS provider can also realize efficiencies in distribution systems, installation, equipment subsidies, billing systems, customer care, and other facilities and functions used by both services.

In contrast, an entrant offering a stand-alone satellite broadband service would be severely constrained by its inability to offer a bundled video service. Accordingly, the creation of a DBS video monopolist – New EchoStar – would result in a de facto satellite

⁸⁹ Salomon Smith Barney 12th Annual Global Entertainment, Media & Telecommunications Conference, Presentation by Jack Shaw, President & CEO, Hughes, and Eddy Hartenstein, President & CEO, DIRECTV (Jan. 8, 2002).

⁹⁰ Application at 6-7.

broadband monopolist as well. Additionally, its substantial control over satellite broadband technology would raise further barriers to entry.

The Commission should not give any weight to the transfer applicants' claim that the merger will "allow New Echostar to proceed with prompt and robust broadband deployment in the Ka-band by spreading the high fixed costs of deployment over a critical mass of broadband subscribers. . . ." ⁹¹ The transfer applicants have not provided any support for their claimed economies of scale, and those claims are contrary to common sense. Economies of scale exist for the provision of a **broadcast** service such as DBS, since an unlimited number of subscribers can be served without needing to add satellite capacity. But no such satellite-driven economies of scale exist for the provision of two-way **broadband** service. Each new subscriber requires proportionately more satellite capacity. Moreover, each merging party, individually, already has a sufficient infrastructure and large nationwide customer base (comparable to the largest cable MSOs). The argument that this merger to monopoly is necessary to allow the deployment of satellite broadband in either rural or urban areas is completely unsupported. Indeed, for all of the reasons discussed above, the effects of the proposed merger on competition in satellite broadband service – potentially the only broadband service that will be available to most rural Americans in the foreseeable future – are unambiguously negative.

⁹¹ Application at 7.

F. Other Non-Cable MVPD Providers Are Not Significant Near-Term Competitors And Thus Would Not Be Effective Constraints On New EchoStar

The transfer applicants have failed to show that new, effective MVPD entry is likely within the near term that would be sufficient to deter the potential anti-competitive effects of the merger.⁹² There are no competitive technologies that hold the promise of entering the market on a time frame or on a scale sufficient to constrain a DBS monopolist. As the Commission just observed in the Eighth Annual Report, “[t]he market for the delivery of video programming to households continues to be highly concentrated and characterized by substantial barriers to entry.”⁹³ While it is possible that new distribution technologies, if accompanied by substantial capital investment, successful execution and consumer acceptance, might at some indeterminate point in the future permit the emergence of new video competition, the transfer applicants have plainly failed to meet their burden of showing that such entry is likely and will offset the demonstrated anti-competitive effects of this merger.

In fact, New EchoStar’s vertical integration in equipment and technology, combined with its monopoly DBS position, will create new barriers to entry. In its antitrust lawsuit against DIRECTV, EchoStar argued that DIRECTV’s contracts with equipment manufacturers were an anti-competitive scheme to monopolize the DBS industry.⁹⁴ The combination of EchoStar and DIRECTV would only intensify the

⁹² See Guidelines, *supra*, § 3.0.

⁹³ Eighth Annual Report, *supra*, ¶ 118.

⁹⁴ See Complaint, *EchoStar v. DIRECTV*, Civ. Action No. 00-212 ¶¶ 155-76 (D. Colo. Feb. 1, 2000).

opportunities for such behavior and impede the ability of new entrants to obtain needed technology.

IV. The Benefits That The Transfer Applicants Claim Will Arise From The Transfer Of Control Are Overstated And Do Not Justify The Elimination Of Competition

A substantial portion of the consolidated transfer application is devoted to the transfer applicants' contentions that the merger will allow increased spectrum and satellite resource efficiency and the deployment of advanced broadband services to all Americans.⁹⁵ Underlying this argument, is the absurd notion that DBS is unable effectively to compete with cable. There simply is no basis for that contention, as the Commission's Eighth Annual Report makes clear. Whether measured by the comparative growth in subscribership between DBS (24%) and cable (1.9%) from July 2000-June 2001, or predictions about DBS' strong prospects for future growth, it is evident that DBS is in a strong competitive position vis-à-vis cable.⁹⁶

While the widespread availability of broadband and other services is certainly a laudable goal, the transfer applicants have failed to prove that the merger is necessary to achieve it. Indeed, as will be shown below, the merger is not necessary to achieve it. Both EchoStar and DIRECTV, as stand-alone entities, are fully capable of achieving this objective today, and they have advanced no evidence to show that they are spectrum-constrained. Moreover, with certain technological enhancements – the costs and

⁹⁵ See Application at 22-35.

⁹⁶ See *Eighth Annual Report* at ¶ 13 (comparing DBS and cable subscribership growth rates); see also *id.* ¶ 56 (discussing Paul Kagan Associates projections for DBS growth, and estimating that DBS subscribership will reach over 28 million by 2010 with \$26 billion in industry revenue).

implementation times of which would not be affected significantly by the merger – both companies, on their own, could provide an even greater array of services and still have ample spectrum for new services that will emerge in coming years. Thus, not only are the alleged benefits of the proposed transfer of control overstated, but also they do not even come close to justifying the harmful effects of this merger (discussed in Section III).

**A. The Most Significant Claimed Benefits Are Readily Achievable
By Both EchoStar and DIRECTV Individually**

Even if one accepts the notion that EchoStar and DIRECTV need to provide an enhanced bundle of services to compete with state-of-the-art digital cable systems, it is clear that each entity has sufficient spectrum today to compete fully on its own.

Both EchoStar and DIRECTV provide DBS service in the high-power BSS band, which is specially allocated and optimized for direct-to-home television broadcasting by international treaty. While more than two dozen C and Ku-band FSS slots are available for full-CONUS service, the United States is assigned just three BSS slots capable of providing full-CONUS service. Thirty-two frequency blocks are available at each slot, for a total of 96 full-CONUS BSS frequencies. EchoStar and DIRECTV, together, control all 96 frequency blocks. EchoStar is licensed to use 50 full CONUS frequency blocks, including 29 frequency blocks at 110°WL and 21 frequency blocks at 119°WL. EchoStar also controls additional spectrum at 61.5°WL, which may be used to provide DBS service to areas east of the Rocky Mountains, and at 148°WL and 175°WL, which may be used to provide DBS service to areas west of the Rocky Mountains. DIRECTV is licensed to use 46 full CONUS frequency blocks, including the entire spectrum at 101°WL (32 frequency blocks), part of the spectrum at 110°WL (3 frequency blocks), and

part of the spectrum at 119°WL (11 frequency blocks).⁹⁷ In addition to their high-power BSS licenses, EchoStar and Hughes have vast amounts of satellite spectrum in other frequency bands which can be used for supplemental broadcasting service and two-way broadband services.⁹⁸

There is no question that EchoStar and DIRECTV each control a substantial amount of spectrum – including more BSS spectrum than they effectively can use today for the provision of DBS service. EchoStar, which notes that it already has “the world’s largest allocation of DBS frequencies,”⁹⁹ uses some of its DBS spectrum for “virtual private television networks,” for delivery of commodity data packages to corporate LANs, and for commercial business television services such as “sales channel education and training,” “corporate news” and “television auctions.”¹⁰⁰ Spectrum scarcity is not what has prevented EchoStar and DIRECTV from providing more local signals, more cable channels, more pay-per-view choices and new enhanced services, and more satellite broadband. Both companies’ platforms are well positioned today to offer a full array of services competitive with, and in many regards superior to, sophisticated digital cable systems. The fact that they have elected not to do so – and to merge rather than to compete – does not serve the public interest and is no reason to allow them to approve the proposed transfer of control.

⁹⁷ See Rusch Aff., ¶¶ 6-7. See also Application at 13.

⁹⁸ See Rusch Aff., ¶ 8.

⁹⁹ See <http://www.businesstelevision.com/technologyframe.html>.

¹⁰⁰ See <http://www.businesstelevision.com/contdelvframe.html>; <http://www.businesstelevision.com/technologyframe.html>.

1. Local Broadcast Retransmission

Hughes and EchoStar claim that the merger is necessary to permit them to provide local broadcast retransmission service to 100 local markets or Designated Market Areas (“DMAs”), and promote this as perhaps the greatest alleged benefit of the merger.¹⁰¹ Currently, EchoStar provides local service to 36 DMAs and DIRECTV provides local service to 41 DMAs, and DIRECTV plans to serve an additional 10 DMAs this year.¹⁰² Thus, giving the transfer applicants the benefit of the doubt, the principal alleged benefit of the merger – and the only one even nominally committed – inures exclusively to the benefit of a small portion of the nation’s DMAs.

The actual net benefit, if there is one at all, is far smaller. As detailed in the attached affidavit and report of Roger J. Rusch, both DIRECTV and EchoStar are already poised to increase greatly the number of DMAs they serve with local broadcast signals, and are fully capable of individually providing local service to 100 DMAs, or to all DMAs. Moreover, they could do so and still provide a suite of national programming, pay-per-view, and other services that are fully competitive with digital cable systems.

To facilitate the carriage of local television broadcasts, DIRECTV and EchoStar have commenced deployment of satellites with multiple “spot beams” to retransmit local television stations to much smaller geographic areas. Because the television signal is transmitted only to a small area, the same frequency may be re-used in other geographic areas without the interference that would result if two signals were transmitted nationally

¹⁰¹ See, e.g., Application at 4, 28.

¹⁰² See Application at 4, 28. See also Press Release, *DIRECTV to Launch Local Channels in 10 New Markets This Year; Local Channels Will Be Available in 51 Markets Representing More Than 67 Percent of U.S. TV Households*, Jan. 8, 2002, available at http://biz.yahoo.com/bw/020108/80450_1.html.

on the same frequency. This means that a single satellite can supply a large number of local television channels with relatively little spectrum usage.

DBS spot beam satellites that are being designed today for this service can reuse the same spectrum 8 to 12 times. As a result, EchoStar and DIRECTV each could distribute all of the eligible local television stations in the top-100 DMAs individually. EchoStar would be required to use only 22% of its full-CONUS DBS spectrum (11 of 50 frequency blocks), and DIRECTV would be required to use approximately 24% of its full-CONUS spectrum (11 of 46 frequency blocks) to provide local-into-local service to the top-100 DMAs.¹⁰³

Therefore, in addition to facilitating local carriage, spot beams make additional spectrum available for nationwide service.¹⁰⁴ As noted, the next generation of DBS satellites – which offer enhanced spot beam usage – are already launched (*e.g.*, the DIRECTV 4S) or under construction.¹⁰⁵

¹⁰³ See Rusch Aff., ¶¶ 11-19.

¹⁰⁴ See Rusch Aff., ¶ 12. These percentages are consistent with those imposed on cable operators. See, *e.g.*, 47 U.S.C. § 534(b)(1)(B) (“A cable operator of a cable system with more than 12 usable activated channels shall carry the signals of local commercial television stations, up to one-third of the aggregate number of usable activated channels on such system.”). With respect to noncommercial education channels, the Communications Act, as amended, provides: “A cable operator of a cable system with a capacity of more than 36 usable activated channels which is required to carry the signals of three qualified local noncommercial educational television stations shall not be required to carry the signals of additional such stations the programming of which substantially duplicates the programming broadcast by another qualified local noncommercial educational television station requesting carriage....” 47 U.S.C. § 535(e).

¹⁰⁵ See Rusch Aff., ¶¶ 13-16. For example, the DIRECTV 4S satellite (launched on November 26, 2001) and the DIRECTV 7S satellite (under construction) will be able to provide local-into-local spot beam service to at least 86 DMAs, and probably the 100 DMAs that New EchoStar claims it will serve, because a number of the spot beams will cover more than one DMA. See *id.* The EchoStar 7, EchoStar 8 and EchoStar 9 satellites should be able to provide comparable service. See *id.* See also Application at 11 (“EchoStar 7, its seventh DBS satellite, equipped with state-of-the-art spot-beam

Footnote continued on next page

Beyond the 100 DMAs that New EchoStar proposes to serve, either entity, on its own, ultimately could serve 150 or all 210 DMAs. It would be entirely feasible to retransmit all of the local television broadcasts in the CONUS¹⁰⁶ with a single satellite or, alternatively, by employing a two-satellite design.¹⁰⁷ The number of frequency blocks needed to provided local-into-local service to various levels of DMAs is set forth in the following table.

# of the Largest DMAs Served	Approximate # of Local TV Stations Entitled to SHVIA Coverage	Approximate # of Frequency Blocks Required	Remaining Non-local Frequency Blocks, DIRECTV	Remaining Non-local Frequency Blocks, EchoStar	Approximate Non-local Frequency Blocks, pre-SHVIA, DIRECTV	Approximate Non-local Frequency Blocks, pre-SHVIA, EchoStar
1-50	610	7	39	43	30	34
1-100	983	11	35	39	30	34
1-150	1277	14	32	36	30	34
1-210	1475	16	30	34	30	34

As illustrated by the foregoing table, the demands of local-into-local coverage on full-CONUS BSS spectrum would not preclude either EchoStar or DIRECTV, on their own, from serving the proposed 100 DMAs today. As compared to service to the top 50

Footnote continued from previous page

technology, is scheduled to launch soon. ECC plans to launch an additional spot beam satellite, EchoStar 8, in the year 2002.”). On January 16, 2002, the FCC’s International Bureau granted EchoStar the authority to launch and operate EchoStar 7 in its 119°WL orbital location. *See In re EchoStar Communications Corp. Application for Minor Modification of DBS Satellite Authorization, Launch and Operating Authority for EchoStar 7, File Nos. SAT-MOD-20010810-00071, SAT-A/O-20010810-00073, Call Sign DBS8801, Order and Authorization, DA 02-118, 2002 WL 54571 (I.B. Jan. 16, 2002).*

¹⁰⁶ For this analysis, Pegasus assumes that 1,475 local television broadcast stations may be eligible for carriage under SHVIA, if EchoStar and DIRECTV were to provide service in all 210 DMAs. *See Rusch Aff.*, ¶ 12 n.2.

¹⁰⁷ The designs for both the single and double satellite systems are explained in the Mr. Rusch’s affidavit. *See Rusch Aff.*, ¶¶ 20-22.

DMAs, service to the next 50 DMAs requires only an incremental four frequency blocks. If both DIRECTV and EchoStar separately launch spot beam satellites designed to provide local television service to the top 100 DMAs, each would still have more frequencies available for non-local (national) services than it did when fewer than 50 local markets were served without spot beams.¹⁰⁸ This approach could be achieved with satellites using the same technology used on the current generation of DBS spot beam satellites, and would be fully compatible with existing set-top boxes.

Of course, EchoStar is already providing retransmission of many local television stations from its partial-CONUS slots. Although EchoStar's approach of bifurcating stations in the same market among multiple slots violates the spirit of SHVIA, consolidating certain markets on non-CONUS slots may be a sensible resolution to any actual spectrum constraints that may emerge in the future, if a single dish solution can be provided to all subscribers in that market. It also is possible for DIRECTV and EchoStar to collaborate on local-into-local service, and thus recognize equivalent spectrum savings, without merging.¹⁰⁹ Doing so would involve relatively minor technical challenges that are already being addressed. EchoStar recently announced it had contracted with Thomson for delivery of DBS receivers that are capable of decoding both the DIRECTV and EchoStar formats.¹¹⁰ Phased, market-by-market introduction of such equipment

¹⁰⁸ See Rusch Aff., ¶ 19.

¹⁰⁹ See, e.g., Andy Pasztor, "Past Meetings Could Snarl Merger of Hughes, EchoStar; FCC, Justice Department Seek Information on Once-Secret Talks and Why They Ended," THE WALL STREET JOURNAL, Feb 4, 2002.

¹¹⁰ See, e.g., Press Release, "Thomson Multimedia and Echostar Sign Manufacturing Agreement for Satellite TV Receivers," Jan. 14, 2002, available at http://biz.yahoo.com/bw/020114/142148_1.html.

would enable a steady migration of customers to a shared local retransmission service, and the orderly reclamation of frequencies used for duplicate retransmissions.

It is thus apparent that, to the extent EchoStar and DIRECTV are not providing local-into-local service to more markets, that is purely a business decision (or a litigation strategy, in light of their efforts to overturn SHVIA), not dictated by spectrum or other technological constraints.

Moreover, even if the Commission approves the pending transfer of control, there is no assurance that New EchoStar actually will provide service to 100 DMAs, let alone all 210 DMAs. Providing service to 100 DMAs (or more) is not a legal requirement. All that is required by SHVIA is that, if a DBS operator carries any local broadcast stations in a market, then it must carry all non-duplicating local broadcast stations in that market upon request.¹¹¹ Indeed, the commitment of EchoStar and DIRECTV to provide greater, much less ubiquitous, local carriage was called into question in the litigation that ultimately affirmed the carry one/carry all requirement.¹¹² Thus, the merger is not

¹¹¹ See 47 U.S.C. § 338(a)(1) (“Subject to the limitations of paragraph (2), each satellite carrier providing, under section 122 of title 17, United States Code, secondary transmissions to subscribers located within the local market of a television broadcast station of a primary transmission made by that station shall carry upon request the signals of all television broadcast stations located within that local market, subject to section 325(b) of this title.”). This commonly is referred to as the “carry one/carry all” requirement. It should be noted that DBS providers have certain carriage exemptions on a market-by-market basis for signals of stations that substantially duplicate the signal of another station within the same local market. See 47 U.S.C. § 338(c).

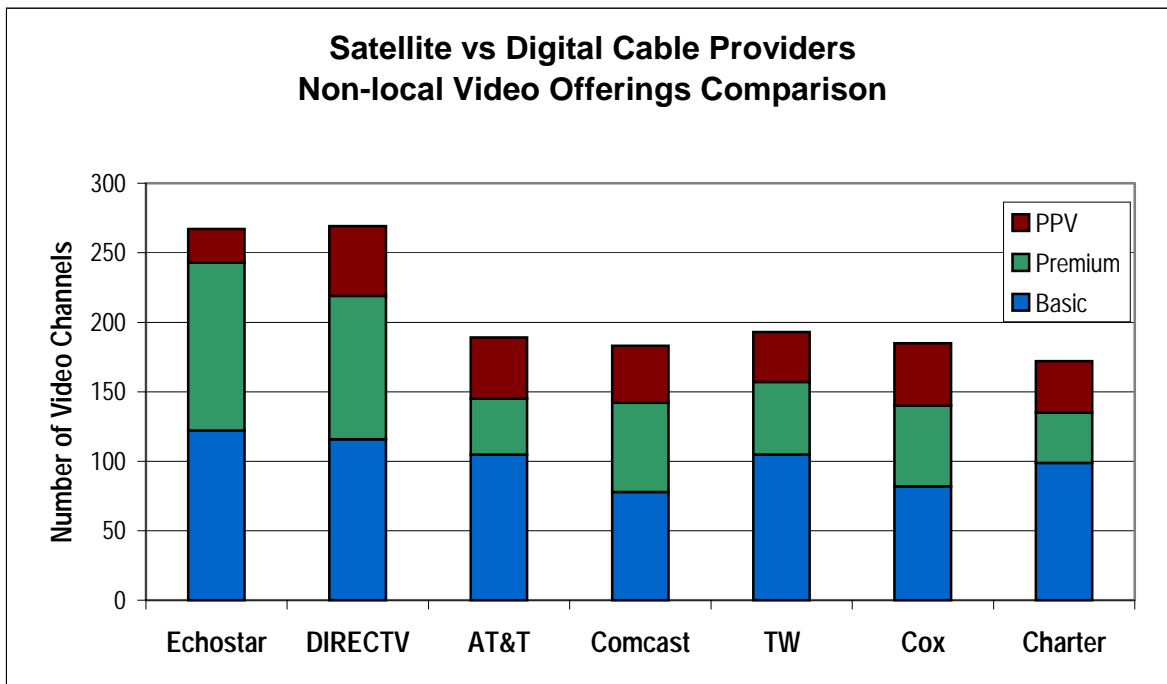
¹¹² “We conclude, then, that both the satellite industry’s track record and its economic incentives provide substantial evidence supporting Congress’ predictive judgment that satellite carriers will deny carriage to significant numbers of independent broadcast stations if the carriers are not bound by the carry one, carry all rule.” *Satellite Broadcasting and Communications Ass’n v. FCC*, 275 F.3d 337, 359 (4th Cir. 2001). The Court also noted that EchoStar and DIRECTV “have plainly announced their intention to continue cherry picking the major network affiliates so long as they may lawfully do so.” *Id.*

necessary to provide local television signals to smaller markets, nor is there any assurance that New EchoStar would do so if the merger is allowed.

2. Additional Programming And Other “Advanced” Services

The transfer applicants’ claim that the merger is necessary to provide additional programming services and more pay-per-view, video-on-demand and similar offerings also is without merit. Indeed, both EchoStar and DIRECTV already provide a line-up of cable channels, as well as ample pay-per-view, video-on-demand, information-on-demand, music, and other services, at a level comparable to digital cable systems. The chart below, compiled from self-reporting sources, shows that DIRECTV and EchoStar today provide substantially more national programming than any major digital cable MSO – and EchoStar has yet to launch its first spot beam satellite.¹¹³ These channels are in addition to the local signals each DBS provider currently retransmits.

¹¹³ Information on channel offerings for DIRECTV and EchoStar taken from presentation by Jack Shaw, President and CEO of Hughes Communications Corp., and Eddy Hartenstein, Chairman and CEO of DIRECTV, at the Salomon Smith Barney 12th Annual Media and Telecommunications Conference, Jan. 8, 2002. Information on channel offerings by AT&T, Comcast, Time Warner, Cox, and Charter compiled from their respective websites on Jan. 30, 2002.



The deployment of spot beam satellites not only will allow the DBS operators to provide local-into-local service to as many local markets as they wish, but it also will “liberate” spectrum that can be employed for the carriage of more national cable video channels,¹¹⁴ as well as to provide pay-per-view, video-on-demand and other service offerings.¹¹⁵ Thus, as with local service, scarcity of spectrum is not an impediment to EchoStar’s and DIRECTV’s provision of these programming services.

3. Satellite Broadband

The transfer applicants argue in the consolidated transfer application that “[t]he merger will allow New EchoStar to provide meaningful broadband competition with cable and telephone companies as a virtual third line into the home for a bundle of

¹¹⁴ As of December 2001, there were 281 national cable video networks in the United States. See Industry Statistics at http://www.ncta.com/industry_overview/indStat.cfm?indOverviewID=2 (last visited Jan. 29, 2002).

¹¹⁵ See Rusch Aff., ¶¶ 27-28.

video/data/Internet services.”¹¹⁶ While increased broadband competition certainly is desirable, this merger is not necessary to achieve it and, indeed, as discussed in Section III.E, would have precisely the opposite effect, particularly in rural America and in other areas where cable modem and/or DSL service is unavailable. In any event, even without regard to the anti-competitive effects the merger would have on the nascent broadband market, it is clear that both EchoStar and DIRECTV already are at the forefront in offering competitive broadband services,¹¹⁷ and that each can and would continue to develop enhanced broadband services on a competitive basis without the merger.

¹¹⁶ Application at i. *See also* Application at 7 (“The proposed combination will allow New EchoStar to proceed with prompt and robust broadband deployment in the Ka-band by spreading the high fixed costs of deployment over a critical mass of broadband subscribers and achieving an offering that combines a competitive price and a reasonably short time to market.”).

¹¹⁷ *See, e.g.*, http://www.dishnetwork.com/content/internet/whats_starband/index.shtml (last visited Jan. 30, 2002) (describing the StarBand service offered by EchoStar); Press Release, “DIRECWAY Subscribers Break 100,000 Mark: Industry Pioneer Hughes Network Systems Continues to Lead Satellite Broadband Market,” Jan. 9, 2002, *available at* http://biz.yahoo.com/prnews/020109/dcw007_1.html (“Hughes Network Systems (HNS) announced today that it has surpassed 100,000 subscribers for its DIRECWAY® broadband satellite service. ‘This is yet another significant milestone that clearly demonstrates HNS’ leadership in the satellite industry. There is a considerable broadband market out there for which DIRECWAY is clearly a winning solution,’ said Pradman Kaul, chairman and CEO of HNS. ‘We are very optimistic about the future and the continued success of DIRECWAY. With all of the business and marketing alliances we have secured, we see enormous potential for growth of DIRECWAY services spanning all markets – enterprise, small business and consumer alike.’”). It is difficult to reconcile this announcement with EchoStar CEO Ergen’s statement that *same day* regarding satellite broadband: “‘Without question, you can go to the bank on this, you’re not going to see satellite broadband without the merger,’ he said.” Ben Berkowitz, *EchoStar Says to Raise Satellite TV Rates 3 pct*, REUTERS, Jan. 9, 2002, *available at* http://biz.yahoo.com/rf/020109/n09302616_2.html.

Both Hughes and EchoStar use competing Ku-band Fixed Satellite Service (“FSS”) platforms for broadband service. EchoStar controls the StarBand system, and Hughes has launched DIRECWAY. These services directly compete with each other.¹¹⁸

Both Hughes and EchoStar also are planning for and investing in advanced satellite broadband platforms using the Ka spectrum.¹¹⁹ Hughes Network Systems sponsors the SPACEWAY project. EchoStar is an investor in WildBlue, “a company that expects to offer high-speed data services at rates up to 1.5 Mbps, beginning in mid-2002” and with which EchoStar plans to develop a receiver capable of receiving both Wildblue’s Internet access and EchoStar’s DBS services.¹²⁰ EchoStar also is constructing EchoStar 9 that carries Ka-band transponders.¹²¹ EchoStar also fought successfully for a waiver of FCC rules permitting it to take majority ownership in and control of Visionstar LLC, which is licensed to use the prime 113°W Ka slot. In petitioning for that approval, EchoStar insisted that it needed additional Ka-band spectrum, and stated that it had a satellite under construction for the slot.¹²² In the transfer application, though, EchoStar argues that the broadband market simply is too speculative and risky to justify a significant investment, and admits that it has only undertaken a single Ka-band satellite, a

¹¹⁸ See Rusch Aff., ¶ 30.

¹¹⁹ See Application at 7-8, 45-49.

¹²⁰ See EchoStar Form 10-K, *supra*, at 5.

¹²¹ See Rusch Aff., ¶ 31. “EchoStar’s first FSS satellite, a hybrid Ku-band/Ka-band satellite, is expected to be launched in 2002.” Application at 11. Collocation of Ka and Ku-band transponders permits customers to use one dish for video and broadband satellite services.

¹²² See *In re Application of VisionStar, Inc., Shant Hovnanian, and EchoStar VisionStar Corp.*, DA 01-2481, 2001 WL 1327105 ¶ 23 (Oct. 23, 2001). See also Letter to Thomas S. Tycz, Chief, Satellite and Radiocommunications Division, International Bureau, FCC, from Michael R. Gardner, Counsel, VisionStar, Inc., and Pantelis Michalopoulos, Counsel, EchoStar VisionStar Corp. (June 7, 2001).

“cautiously modest project equipped with only a limited number of spot beams designed to serve only a few geographical areas in the United States.”¹²³ The Commission carefully should compare the vague language of the transfer application with the transfer applicants’ previous commitments.

Both EchoStar and Hughes each have sufficient spectrum (both in the Ku FSS and Ka FSS bands) to offer a competitive broadband service.¹²⁴ Moreover, both have existing customer bases accustomed to using satellite services, vast distribution networks, and formidable financial resources necessary to support satellite broadband through the growth phase. Permitting the companies to join forces will not accelerate the pace of satellite broadband deployment and, for the reasons explained in Section III.E, will hinder advancements by eliminating one of the two currently operating platforms and one or more of the advanced platforms the two companies are sponsoring.

B. Both EchoStar And DIRECTV Could Make Even More Efficient Use Of The Ample Spectrum That Each Currently Controls With Certain Technological Improvements

The transfer applicants’ complaints of inadequate spectrum are unfounded, as are their claims that the spectrum they have today can never yield greater capacity. The capacity of spectrum is not fixed; it is a function of the technology employed. DIRECTV and EchoStar, like all users of satellite, terrestrial, wired, and wireless spectrum, always have the option of future capacity growth by upgrading the technology that defines their networks. Technological upgrades are expensive and complex, but they are achievable when the market demands them, and can be effectuated incrementally, without disturbing

¹²³ Application at 46.

¹²⁴ See Rusch Aff., ¶ 32. See also *infra* at Section V.B.1.

the installed base. Large urban cable systems have upgraded their infrastructure at least twice – from low-capacity analog to high-capacity analog and, finally, to digital. The digital upgrade required an almost complete change-out of headend equipment, extensive line upgrades, and the distribution of new boxes to consumers opting for digital services. If EchoStar or DIRECTV one day need more capacity to compete with future iterations of digital cable, then they too can upgrade their plant to implement any number of techniques that vastly can improve overall capacity.

Some of the available technological enhancements available today include: turbo coding; 8PSK; improved compression; and personal video recorders. Each feature, along with its ability to increase capacity, is described below.

- Turbo coding. Turbo coding is currently being used on some satellite services to improve the signal robustness (lowering the required Eb/No) substantially, by as much as a factor of two. Effective use of turbo coding could double the effective channel capacity of a satellite.¹²⁵
- 8PSK modulation. Higher-order modulation makes possible transmission at higher data rates using the same frequency bandwidth. This is the same technique that has been used to transmit higher data rates over telephone lines and cable television. At present, most of the DBS modulation is called Quaternary Phase Shift Keying (QPSK or 4PSK), but 8PSK could be used instead. Using 8PSK would increase the transmission data rate, and therefore the number of channels carried in each frequency, by about 35%.¹²⁶
- Improved compression. DIRECTV and EchoStar today use the MPEG-2 standard for video compression, which enables data rates of about 2-3 Mbps for standard definition television pictures. The recently adopted MPEG-4 standard can provide a reduction in data rates by a factor of two or three as compared to MPEG-2.¹²⁷ (Although use of improved compression technology might require

¹²⁵ See Rusch Aff., ¶ 35.

¹²⁶ See Rusch Aff., ¶ 36-37.

¹²⁷ See Rusch Aff., ¶ 38-39.

changes to the transmission equipment and the set-top box, it seems likely that the transfer applicants will undertake equipment changes in any event.)¹²⁸

- Personal video recorders. The advent of personal video recorders (“PVRs”) can both ease spectrum demands and provide consumers with greater programming flexibility. Such devices, which readily can be incorporated in set-top boxes, allow consumers to capture programming and watch it whenever they wish. Obviously, this is an attractive service for consumers but, in terms of spectrum needs, it also benefits EchoStar and DIRECTV. For example, rather than using four channels to broadcast the same pay-per-view movie over and over with staggered start times, as DIRECTV typically does, the movie can be transmitted just once and “captured” by consumers’ PVRs. The DBS provider recognizes a 96% improvement in spectrum efficiency and the consumer can have any start time she wishes.¹²⁹

By adopting any or a combination of the foregoing technologies, each company would have more spectrum available for new services. However, if EchoStar and DIRECTV merge, the competitive pressures to innovate to achieve greater spectrum efficiency will be eliminated.¹³⁰ That would be inconsistent with the public interest.

C. There Is Not A Meaningful Difference In The Costs And Time Associated With Implementing Expanded Local-Into-Local Service And Maximizing The Efficient Use Of Spectrum Between EchoStar And DIRECTV Individually, And New EchoStar As A Merged Entity

If EchoStar and DIRECTV merge, they will not eliminate many of the expenses associated with bringing local service to more DMAs or augmenting spectrum efficiency.

¹²⁸ See, e.g., Press Release, “Thomson Multimedia and Echostar Sign Manufacturing Agreement for Satellite TV Receivers,” Jan. 14, 2002, available at http://biz.yahoo.com/bw/020114/142148_1.html.

¹²⁹ See Rusch Aff., ¶¶ 40-42. EchoStar recently has been involved in various efforts to expand its customers use of PVRs. See, e.g., Press Release, “DISH Network to Introduce New, Improved Personal Video Recorder: DishPVR 508 Satellite TV Receiver,” Jan. 9, 2002, available at http://biz.yahoo.com/bw/020109/90169_1.html; Press Release, “Moxi Digital and EchoStar Collaborate on Advanced Software Platform For Satellite TV Set-Top Boxes: Moxi Demonstrates Its Complete Solution for Distributing Entertainment Throughout the Home,” Jan. 7, 2002, available at http://biz.yahoo.com/prnews/020107/hsm027_1.html.

¹³⁰ Thus, the transfer applicants are mistaken to assert that the merger will promote “efficient use of scarce spectrum.” Application at 3. Indeed, the opposite is true.

The transfer applicants acknowledge that it will take time and substantial resources even to realize the benefits they claim will result from the merger.¹³¹

Pegasus does not dispute that increasing the provision of local-into-local service and developing new spectrum-efficient technologies¹³² will require the expenditure of financial and other resources. There are likely to be expenses associated with new satellites and ground station facilities, as well as necessary upgrades to CPE. For example, in order to offer expanded local-into-local service, some customers' existing antennas will need to be repositioned to point to another satellite. In addition, a number of the suggested spectrum-efficiency technological improvements will require set-top box modifications.¹³³

Although these – and, perhaps, other – costs will be unavoidable if EchoStar and DIRECTV want to maximize the efficiency of their spectrum and deliver improved services, there does not appear to be a meaningful distinction between the costs that would be incurred by New EchoStar, on the one hand, and the individual companies vigorously competing, on the other hand. Assuming the merger is consummated, New EchoStar will need to integrate its combined customer base on a common platform.¹³⁴ This means providing new set-top boxes for those users that would change from the EchoStar signal format to the DIRECTV format (approximately 7 million users) or vice versa (approximately 11 million users). Moreover, many of the users would require new

¹³¹ See generally Willig Declaration at 13 n.18; Joint Engineering Statement to the Application at 2-7.

¹³² See Section III.B, *supra*.

¹³³ See Rusch Aff., ¶¶ 43-45.

¹³⁴ See Joint Engineering Statement at 3.

antennas for local-into-local service, depending on how the system ultimately is configured.¹³⁵ Mr. Rusch concludes:

Whether EchoStar and DIRECTV merge or pursue upgrades individually, the costs are significant. It is not obvious that there are any additional upgrade cost efficiencies for a merged company. The costs and processes are essentially the same.

Consequently, there is not likely to be a measurable difference in the completion time and the costs involved if EchoStar and DIRECTV pursue upgrades individually or as a merged entity.¹³⁶

Thus, any merger-specific cost benefit associated with facilities and equipment upgrade is, at best, minimal, and surely not of a sufficient magnitude to offset the competitive harms that will result from the proposed transfer of control. Indeed, the merger simply will give New EchoStar more freedom to pass these inevitable expenses through to customers, comfortable in its knowledge that the corresponding price increase will not be constrained by the pressures currently exerted by EchoStar and DIRECTV on one another.

V. The Other Claimed Benefits Of The Merger Are Illusory

The transfer applicants maintain that combining their companies will lead to a variety of benefits beyond more local-into-local and satellite broadband service. Upon examination, though, it is evident that these purported benefits are illusory.

A. Uniform “National Pricing” Is An Empty Promise

The transfer applicants have recognized that their merger will eliminate MVPD competition for millions of consumers, primarily in rural areas. They have sought to

¹³⁵ See Rusch Aff., ¶ 46.

¹³⁶ See Rusch Aff., ¶ 48-49.

allay the natural concerns this would raise by promising to offer uniform “national pricing” for DBS service.¹³⁷ The Commission should view this supposed benefit of the merger with skepticism.

This assertion – which is not embodied in any form of a binding commitment – actually raises more questions than it answers.¹³⁸ For example: What happens to this proposal if New EchoStar decides to change its plans? How would the pricing be set? Will the new national price be higher than current DBS prices, since even in urban and suburban areas New EchoStar will be operating in at best a duopoly market? Who would enforce national pricing? How, if it all, would it be enforced? How long would it be in effect? How does it relate to pricing for promotions, special packages and regional sports offerings?¹³⁹ Does it mean that charges will be the same throughout the United States for local-into-local service in different markets? What impact does it have on installation, repair and CPE prices?

¹³⁷ See, e.g., Application at ii, 42; *Cable and Satellite Broadcast Competition: Hearing Before the House Judiciary Committee*, 107th Cong. (2001) (statement of Charles W. Ergen, Chairman and CEO, EchoStar Communications Corp.).

¹³⁸ The non-binding nature of the national pricing commitment is reminiscent of AOL’s and Time Warner’s efforts to assuage the Commission’s and interested parties’ concern about the ability of unaffiliated Internet Service Providers (“ISPs”) to gain access to Time Warner’s cable systems. See generally *AOL/Time Warner Order*, *supra*, ¶ 91 (discussing AOL’s and Time Warner’s joint Memorandum of Understanding (“MOU”) in which they voluntarily committed to negotiate for unaffiliated ISPs to connect to Time Warner’s cable systems on a non-discriminatory basis). The Commission concluded that the MOU, while well-intentioned, did not suffice because the MOU, on its own, was “not legally enforceable.” See *id.* ¶¶ 93-96. Here, the voluntary and unenforceable nature of the national pricing promise is one of its many flaws.

¹³⁹ Regionalized pricing can and does occur today within the DBS industry. DBS providers have run special regional promotions. See *Willig Aff.*, ¶ 28 n.25 (“[B]oth firms, in fact, have offered temporary local promotions on installation and equipment in the past.”). In 1996, EchoStar ran a regional trial promotion on equipment fees before offering it on a national basis. See, e.g., *Echostar Communications Corp: Special Satellite Package Offered in Selected Markets*, WALL ST. J., June 7, 1996.

None of these questions have been addressed by the transfer applicants. Moreover, the implication that this will lead to lower prices is, at best, speculative.¹⁴⁰ The real impact of national pricing is likely to be higher prices for consumers. In any given market, New EchoStar's incentive to engage in aggressive price competition with the cable operator will be reduced because, if New EchoStar is to maintain national pricing, the reduction of prices in one market would require an across-the-board reduction throughout the United States. Thus, New EchoStar will be reluctant to reduce prices anywhere if it is faced with the prospect of doing so everywhere. Further, the national pricing plan does not even pretend to address many of the harms to consumers arising from the loss of DBS competition which, as set forth in Section III.D.1, include the benefits of competition in pricing trends, equipment pricing, packages, programming, promotions, bounty programs, innovation, and distribution networks.

In sum, once one looks behind the veneer of uniform national pricing, it is apparent that all that is offered is an unenforceable promise, subject to change at New EchoStar's desire, that may be an impediment to downward pressure on DBS pricing. It is, therefore, apparent that national pricing is not a substitute for meaningful competition.

B. Many Of The Purported Efficiencies Will Have No Consumer Benefits

The transfer applicants also claim a number of other benefits will result from the merger. Here too, the transfer applicants have failed to prove by a preponderance of the evidence that these benefits will materialize or, in any event, that they are merger-specific or will benefit consumers. The Commission has made clear that in assessing whether

¹⁴⁰ See Application at 42.

efficiencies will offset a reduction in competition from a merger, it will take account of only those efficiencies that will provide benefits that will inure directly to consumers.

Applicants have not demonstrated, or even stated, that these cost savings would be passed through to consumers in the form of lower prices or new or improved services. . . . [T]he absence of explicit pass-throughs committed to by the Applicants renders it difficult to evaluate the extent to which actual cost savings would benefit the public interest. Additionally, [the Applicants] provide little detail regarding their claimed efficiencies. Although the Applicants have indicated the various sources of the claimed savings, the record nonetheless lacks sufficient evidence to support those claimed cost savings. As a result, we find it difficult to evaluate the Applicants' claims and find them unpersuasive.¹⁴¹

In addition to the purported spectrum efficiencies discussed above, the transfer applicants claim that the merger will provide cost savings through reduced subscriber acquisition costs; reduced customer turnover, or “churn”; improved signal security from a standardized platform; reduced programming costs; and elimination of duplicative overhead.¹⁴² They make no attempt, however, to show how these claimed savings will be passed on to consumers, and it is by no means obvious that they would.

Indeed, the most substantial of these so-called efficiencies – reduced subscriber acquisition costs and reduced churn¹⁴³ – appear to be the direct product of eliminating competition and will be harmful rather than beneficial to consumers. A reduction in

¹⁴¹ *GTE-Bell Atlantic Order, supra*, 14,142, ¶ 242 (emphasis added).

¹⁴² See Application at 36.

¹⁴³ In presentations to the investor community, the transfer applicants have indicated that “reduced subscriber acquisition costs” account for \$900 million to \$1.2 billion of the claimed cost savings, or over one-third, and reduced churn accounts for \$750-850 million. See EchoStar Communications Corp., General Motors Corp., and Hughes Electronics Corp., Webcast Announcing Merger, available at <http://216.167.43.201/EchoStar-Hughes-.PDF>.

subscriber acquisition costs presumably refers to what the DBS providers now spend on promotions, equipment subsidies, and price reductions that each competitor has to offer to entice customers away from the competitive DBS product. As Dr. Rubinfeld states, a reduction in the costs associated with acquiring subscribers may lead to an increase in the effective price that consumers pay for DBS service.¹⁴⁴ Similarly, reduced churn is simply another way of saying that customers will not have another DBS choice and thus will be forced to stay with New EchoStar even if the price goes up or service is degraded.

Many other efficiencies cited by the transfer applicants simply are not merger-specific, and thus should not be considered by the Commission.¹⁴⁵ “[E]fficiencies that can be achieved through means less harmful to the public interest than the proposed merger cannot be considered true benefits of the merger.”¹⁴⁶ Moreover, there is no basis upon which the Commission could conclude that these efficiencies would be shared with consumers. A few additional examples, in particular, illustrate this fundamental shortcoming in the Application.

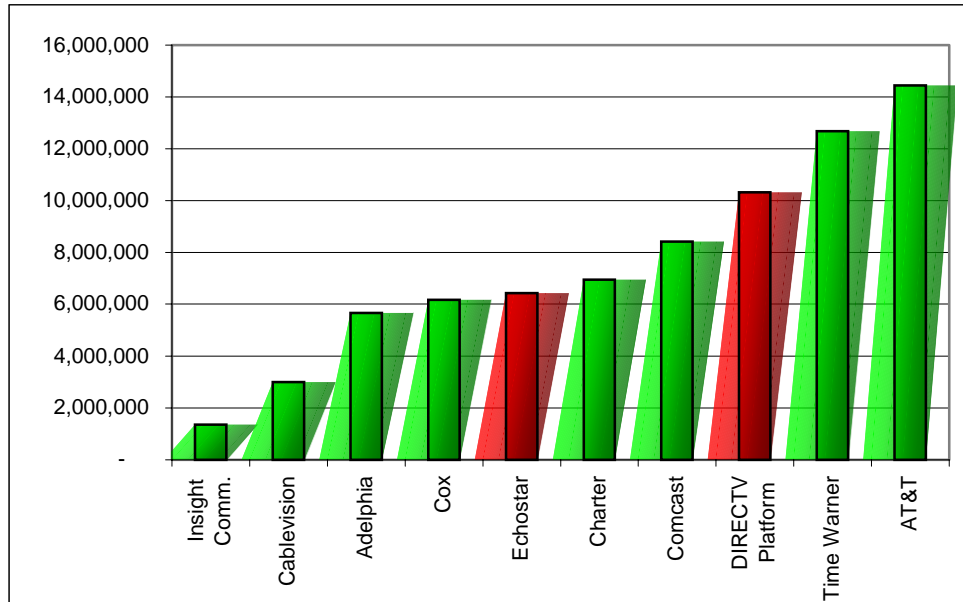
First, the transfer applicants suggest that, as a combined entity, they will be able to obtain programming on better terms and conditions than either EchoStar or DIRECTV

¹⁴⁴ See Rubinfeld Aff., ¶ 48.

¹⁴⁵ See *GTE-Bell Atlantic Order*, *supra*, at 14,141 ¶ 239 (“Based upon the evidence in the record, we conclude that the Applicants have not demonstrated *that the efficiencies and cost savings that they contend will result from the merger are merger-specific or will mitigate the competitive harms* discussed above.”) (emphasis added).

¹⁴⁶ *Id.* at 14,141 ¶ 240.

can on its own.¹⁴⁷ DIRECTV is larger than all but two MSOs, and EchoStar is the sixth largest MVPD provider in the United States, as illustrated by the following chart.¹⁴⁸



US Subscribers for Top 8 MSOs and DBS Platforms (in thousands)

The transfer applicants have not shown that they are unable to obtain programming at competitive prices.¹⁴⁹ Indeed, even a cursory review of each company's

¹⁴⁷ See Application at 36 (an alleged cost synergy from the merger is "reduced programming costs as a result of having a larger subscriber base.").

¹⁴⁸ The MSO subscriber information in these charts was obtained from the 2001 Warren Cable Factbook, and the information on EchoStar and DIRECTV subscribers was reported by the companies as of September 30, 2001. Following the merger, New EchoStar would be larger than any cable MSO.

¹⁴⁹ For example, Disney's recent lawsuit against EchoStar with respect to carriage of the ABC Family channel illustrates the leverage vis-a-vis programmers that EchoStar already exercises. See *International Family Entm't, Inc. v. EchoStar Satellite Corp.*, Case No. 01-1087 8 GAF (C.D. Cal.) (complaint filed Dec. 20, 2001). See also Richard Verrier, *Reprieve For Disney's ABC Family; Courts: Judge Issues A Temporary Restraining Order To Stop Satellite-TV Provider From Dropping The Channel*, L.A. TIMES, Jan. 1, 2002, at C2. This leverage was further evidenced by EchoStar's decision to drop carriage of another Disney affiliate, ESPN Classic, when the carriage agreement expired at the end of 2001. See Bruce Orwall, *Court Orders EchoStar To Keep Carrying Disney's ABC Family Channel On Satellite*, WALL ST. J., Jan. 2, 2002, at C17.

current channel lineups reveals that both are already providing a channel lineup that is similar to the large cable MSOs.¹⁵⁰ To the extent that, as a merged entity, New EchoStar will enjoy greater leverage with programmers, that would be due to the exercise of monopsony power by what would be the nation's dominant DBS provider and, in most rural areas, a monopoly MVPD. In any event, even if the transfer applicants had provided evidence in support of this contention, there is no binding commitment that the cost savings associated with more favorable program carriage agreements would be shared with consumers.

Second, the transfer applicants also maintain that the merger will allow them to provide a new array of services – foreign language, other niche programming, and educational programming.¹⁵¹ As discussed in Section IV.A, there is no spectrum or other technological constraint preventing each of EchoStar and DIRECTV individually from providing these services today if they are genuinely interested in doing so. Further, and not surprisingly, as with their other “commitments,” these benefits are presented in a conclusory fashion and are not underwritten by any sort of binding agreement to do what is promised. Once again, the Commission should afford these voluntary offers little, if any, weight when balanced against the competitive harms presented by the proposed transfer of control.

¹⁵⁰ Compare EchoStar Channel Lineup, at <http://204.95.170.116/dishsite/listings/lineup.asp>, DIRECTV Channel Lineup, at <http://www.directv.com/programming/programmingpages/0,1093,176,00.html>, Comcast, Montgomery Co., MD, Channel Lineup, at <http://www.comcast.com/cablesys/defaultframe.asp>, and Time Warner– NYC Channel Lineup, at <http://www2.twnyc.com/index2.ftcs.cfm?c= dtv/channel&startrow=11&lessby=1&endrow=20&area=NM> (all last visited Jan. 25, 2002).

¹⁵¹ See Application at 34-35.

Third, the transfer applicants place heavy reliance on the unsubstantiated argument that by consolidating the entire full-CONUS DBS spectrum, customers, services and infrastructure in a single firm, the merger will make DBS a more effective competitor to cable. They claim the imminent availability of video on demand service on digital cable “has emerged as the silver bullet to DBS” and will inevitably lead to greater domination by cable.¹⁵² But, before this merger was announced, DIRECTV was reported saying that it “does not fear losing customers to the increased rollout of digital cable.”¹⁵³ The company noted that its churn rates in areas with digital cable were no more significant than DIRECTV’s overall churn rate of 1.7%.¹⁵⁴

Nor is digital cable taking the country by storm. Only 20% of all cable subscribers currently have digital service.¹⁵⁵ Churn rates for digital cable are significantly higher than the rest of the industry. A 2001 Horowitz Assoc. and S. Liebmann & Assoc. study estimated digital cable churn rates at 5-8% compared to an average of 1.8% for DBS.¹⁵⁶ Similarly, video on demand is not generally available, and the DBS providers are already preparing to offer it. As of June 2001 nearly all of the MSOs were still just in the trial phase for video on demand services. Forrester Research has suggested that video on demand will not have an impact on DBS churn until 2006 at

¹⁵² Application at 26.

¹⁵³ *No Digital Cable Envy for DIRECTV*, CABLE WORLD, Apr. 23, 2001.

¹⁵⁴ *See id.*

¹⁵⁵ *See Eighth Annual Report, supra*, ¶ 38.

¹⁵⁶ *Canadian Ownership Review*, TELEVISION DIGEST, June 11, 2001; *Churn that Burns*, CABLE WORLD, Mar. 19, 2001 (describing digital cable churn as “cable’s dirty little secret” and noting that many customers are disconnecting digital cable after the end of promotional periods).

the earliest (and appears to assume no advances in available similar DBS services).¹⁵⁷

Moreover, EchoStar already has arranged to gain access to video on demand technology through its relationship with Vivendi. Thus, the merger is not necessary to allow DBS to withstand a competitive threat from digital cable, and is instead likely to blunt the competition that DBS, as an upstart technology, had provided in the MVPD market.

Finally, EchoStar's new relationship with Vivendi highlights the fact that many, if not all, of the claimed efficiencies could be achieved by joint-venturing or some other means. For example, through the Vivendi agreement, EchoStar plans to carry expanded pay-per-view and video on demand movies, as well as other interactive games, movies sports and music.¹⁵⁸

VI. The Proposed Merger Violates Established Commission Policy Precluding Excessive Concentration of Spectrum or Orbital Locations By One Entity and Will Lead to Spectrum Warehousing

The Commission has unique responsibility for management of the radio-frequency spectrum.¹⁵⁹ In that role, it routinely decides to limit the amount of spectrum that any one entity may be licensed to use in a particular service.¹⁶⁰ The Commission

¹⁵⁷ *Adding Interactive Services Will Cut Cable Churn*, CABLE WORLD, May 7, 2001.

¹⁵⁸ See EchoStar Communications Corp. Form 8-K (filed with Securities & Exchange Comm'n Dec. 14, 2001).

¹⁵⁹ 47 U.S.C. §§ 301, 303.

¹⁶⁰ See, e.g., *In re Establishment of Rules and Policies for the Digital Audio Radio Satellite Service in the 2310-2360 MHz Frequency Band*, Report and Order, Memorandum Opinion and Order, and Further Notice of Proposed Rule Making, 12 FCC Rcd. 5,754, 5,756 ¶ 3 (1997) (prohibiting consolidation of DARS licenses); *In re Rulemaking to Amend Parts 1, 2, and 25 of the Commission's Rules to Redesignate the 27.5-29.5 GHz Frequency Band, to Reallocate the 29.5-30.0 GHz Frequency Band, to Establish Rules and Policies for Local Multipoint Distribution and for Fixed Satellite Services*, 12 FCC Rcd. 22,310, 22,320, ¶ 24 (1997) (limiting initial orbital assignments for FSS operators to two); *Implementation of Sections 202(a) and 202(b)(1) of the Telecommunications Act of 1996*, 11 FCC Rcd. 12,368, 12,369, ¶ 3 (1996) (limiting the number of radio stations a licensee may have per market); *Review of the Commission's Regulations Governing Television Broadcasting, Television Satellite Stations Review of*

Footnote continued on next page

typically makes that decision based primarily on its determination of the minimum amount of spectrum that a licensee needs to offer a viable service.¹⁶¹ In the only case in which the Commission has permitted licensing of one applicant for a nationwide service, it has required the licensee to operate as a common carrier.¹⁶² Granting the pending transfer application would be inconsistent with that well-reasoned policy.

Footnote continued from previous page

Policy and Rules, 16 FCC Rcd. 1,067, 1,068-79, ¶¶ 3-36 (2001) (limiting ownership of television stations to, at most, two per market).

The Commission has relaxed restrictions only where it has determined that restrictions are impeding the ability of licensees to be competitive or where competition has flourished and the restrictions have become unnecessary. *See, e.g., In re 2000 Biennial Regulatory Review, Spectrum Aggregation Limits for Commercial Mobile Radio Services*, FCC 01-328, ¶ 47 (Dec. 18, 2001); *In re Revision of Part 22 And Part 90 of the Commission's Rules to Facilitate Future Development of Paging Systems, and Implementation of Section 309(j) of the Communications Act—Competitive Bidding*, 12 FCC Rcd. 2,732, 2,777-78, ¶ 88 (1997); *In re Amendment of Parts 21, 43, 74, 78, and 94 of the Commission's Rules Governing Use of the Frequencies in the 2.1 and 2.5 GHz Bands Affecting: Private Operation-Fixed Microwave Service, Multipoint Distribution Service, Multichannel Multipoint Distribution Service, Instructional Television Fixed Service, and Cable Television Relay Service*, 5 FCC Rcd. 6,410, 6,411 ¶ 8 (1990).

¹⁶¹ *See, e.g., Amendment of the Commission's Rules Regarding Installment Payment Financing for Personal Communications Services (PCS) Licensees*, 15 FCC Rcd. 16,266, 16,273, ¶ 12 (2000); *In re Establishment of Rules and Policies for the Digital Audio Radio Satellite Service in the 2310-2360 MHz Frequency Band*, 12 FCC Rcd. 5,754 5,771-72, ¶¶ 41, 42, 49 (1997); *In re Amendment of the Commission's Rules to Establish Part 27, the Wireless Communications Service ("WCS")*, 12 FCC Rcd. 10,785, 10,807-08, ¶ 45 (1997); *In re Amendment of Part 90 of the Commission's Rules to Facilitate Future Development of SMR Systems in the 800 MHz Frequency Band*, 11 FCC Rcd. 1,463, 1,489, ¶ 36 (1995); *In re Amendment of Parts 2, 21, 87, and 90 of the Commission's Rules to Allocate Spectrum for, and to Establish Other Rules and Policies Pertaining to, the Use of Radio in Digital Termination Systems for the Provision of Digital Communications Services*, 86 FCC 2d 360, 373, 386, ¶¶ 35, 67 (1981); *Amendment of Parts 1, 2, 21, and 43 of the Commission's Rules and Regulations to Provide for Licensing and Regulation of Common Carrier Radio Stations in the Multipoint Distribution Service*, 45 FCC 2d 616, 622 ¶ 15 (1974).

¹⁶² *See In re Amendment of Parts 2, 22, and 25 of the Commission's Rules to Allocate Spectrum for and to Establish Other Rules and Policies Pertaining to the Use of Radio Frequencies in a Land Mobile Satellite Service for the Provision of Various Common Carrier Services*, 2 FCC Rcd. 485, 490 ¶ 34 (1987).

It would result in a single entity holding all of the full CONUS Ku-band DBS orbital locations, contrary to established Commission policies designed to assure a competitive DBS marketplace. Moreover, if the merger is approved, New EchoStar would control more Ka-band orbital locations than it conceivably could use in the foreseeable future. Together with its monopoly of the Ku-band DBS spectrum, New EchoStar would thus be able to exercise disproportionate power in the satellite broadband marketplace, thereby depriving the public of the benefits of the new services and the more efficient use of spectrum which a competitive marketplace would produce.

A. Contrary to Commission Policy, New EchoStar Would Control All DBS Full-CONUS Orbital Locations

When the Commission adopted its DBS rules, it decided that, because of the uncertainty as to how the DBS business would develop, it would regulate with a light hand in order to foster open entry. The Commission reasoned that by minimizing regulatory restrictions, the DBS industry would develop in response to market demand and would not be constrained by artificial rules.¹⁶³ Thus, the Commission did not impose any ownership limitations or limit the number or type of orbital locations a single DBS operator might hold. The FCC's decision to refrain from imposing a rigid regulatory structure on the emerging DBS market was made in the expectation of "considerable

¹⁶³ See *In re Inquiry into the Development of Regulatory Policies in Regard to Direct Broadcast Satellites for the Period Following the 1983 Regional Admin. Radio Conference*, Report and Order, 90 FCC 2d 676, 707-08 ¶ 81 (1982) ("DBS Report & Order") ("Imposing minimal regulation will also allow us to gather information about the operation of the industry, which will allow us to make better-informed decisions about permanent regulatory policies."), *recon. denied*, 53 Rad. Reg. 2d (P & F) 1637 (1983), *aff'd in part and vacated in part*, *Nat'l Ass'n of Broadcasters v. FCC*, 740 F.2d 1190 (D.C. Cir. 1984).

competition among DBS systems.”¹⁶⁴ The Commission believed that “if a large number of DBS channels prove viable . . . several DBS operators will compete among themselves and with terrestrial suppliers to provide video services.”¹⁶⁵ And, when the Commission authorized multiple initial DBS operators,¹⁶⁶ it assigned each applicant spectrum in multiple DBS slots,¹⁶⁷ thereby assuring that each authorized DBS operator could provide a competitive service.

Since that time, the Commission has held that the three full-CONUS slots – 101°WL, 110°WL, and 119°WL – are far more desirable¹⁶⁸ than the five half-CONUS slots,¹⁶⁹ and that operation from those full-CONUS slots is essential to any effective DBS

¹⁶⁴ See *DBS Report & Order*, *supra*, at 712 ¶ 95 (addressing competition for programming). See also *id.* at 697-98 ¶¶ 57-58 (reporting that the FCC had accepted for filing nine DBS applications representing a “wide variety of system designs, service offerings, and spectrum requirements” and that three additional applications were on file).

¹⁶⁵ *DBS Report & Order*, *supra*, at 712 ¶ 95.

¹⁶⁶ See *In re Applications of CBS, Inc., et al.*, Memorandum Opinion and Order, 92 FCC 2d 64 (1982).

¹⁶⁷ See *In re Policies and Rules for the Direct Broadcast Satellite Service*, Notice of Proposed Rule Making, 13 FCC Rcd. 6,907, 6,913 ¶ 7 (1998).

¹⁶⁸ Although Section 100.13 of the Commission’s rules provides that all orbital slots will be treated as equal to each other, it is clear that that rule was adopted in order to avoid the necessity of conducting a comparative hearing among DBS applicants as long as there are sufficient orbital slots to allow the Commission to grant all of the pending applications. Cf. *In re Petition and Application of Tempo Satellite, Inc.*, Memorandum Opinion and Order, 7 FCC Rcd. 6,597, 6,598 ¶ 6 (1992) (rejecting Tempo’s claim that, because it applied for the same orbital locations as other DBS applicants and all orbital positions are not equivalent, it was entitled to a comparative hearing). See also *In re Amendment of Parts 2, 22 and 25 of the Commission’s Rules to Allocate Spectrum for and to Establish Other Rules and Policies Pertaining to the Mobile Satellite Service for the Provision of Various Common Carrier Services*, Tentative Decision, 6 FCC Rcd. 4,900, 4,904-05 ¶¶ 19-23 (1991) (discussing the FCC’s “longstanding and deliberate policy” of avoiding comparative hearings to allocate satellite authorizations because the FCC’s established view that “the unique characteristics of the satellite service render it infeasible to select satellite licensees through comparative hearings”).

¹⁶⁹ See *In re Applications of Continental Satellite Corp., et al.*, Memorandum Opinion and Order, 4 FCC Rcd. 6,292, 6,293-94 ¶¶ 7-10 (1989).

operation.¹⁷⁰ Service from the “half-CONUS” or wing slots can be used to supplement service from the full-CONUS slots or provide niche services, but they cannot be used to compete effectively with the DBS operations from the full-CONUS slots.¹⁷¹ As the Commission stated in rejecting arguments that EchoStar’s acquisition of the half-CONUS slots initially assigned to Direct Broadcasting Satellite Corporation would give EchoStar excessive control over orbital allocations:

An operator using two partial-CONUS locations, whether providing a single national service or two separate regional services, would face significant disadvantages in competing with services offered from full-CONUS orbital locations. DBS services are characterized by very high fixed and sunk cost investments, particularly those costs associated with the construction and launch of satellites. Therefore, an operator seeking to combine two partial-CONUS locations to offer a single national service would incur substantially greater costs than would a full-CONUS operator. If the two partial-CONUS locations are used instead to provide separate regional services, the operator would face the analogous problem of having smaller bases of potential subscribers over which to spread those fixed and sunk costs because neither location can be used to offer service to the

¹⁷⁰ See *In re Revision of Rules and Policies for the Direct Broadcast Satellite Service*, Report and Order, 11 FCC Rcd. 9,712, 9,729 ¶ 44 (1995) (“*DBS Auction Order*”) (stating that the potential “number of DBS firms is necessarily limited by the number of full-CONUS orbital locations”). EchoStar itself has acknowledged, in its recent letter requesting additional time to commence construction of its Ku-band satellite to operate at 148°WL, that operation from a full-CONUS location is essential for the efficient provision of local-into-local service. See Letter to Magalie Roman Salas, Secretary, FCC, from David K. Moskowitz, Senior V.P. & General Counsel, EchoStar Satellite Communications Corp. (Jan. 8, 2002).

¹⁷¹ For example, R/L DBS, which holds eleven half-CONUS DBS channels, claims that “it was difficult to develop a viable DBS service that could compete with the two dominant players in the DBS market DirecTV and Echostar. . . . [and thus] [i]n order to compete, R/L DBS . . . must service a niche market not being served by the current DBS providers.” *In re Petition of R/L DBS Company, L.L.C. for Extension of its Direct Broadcast Satellite Constr. Permit*, Memorandum Opinion and Order, 16 FCC Rcd. 9, 13 ¶¶ 12, 16-17 (2000) (granting an extension of the milestone deadlines in part because R/L DBS overcame difficulties to build out its niche half-CONUS service in face of competition in “current DBS market, which is dominated by two companies offering up to 350 channels of video programming”).

entire United States. As a result, partial-CONUS DBS operations appear likely to involve higher per-subscriber costs of operation than do full-CONUS DBS operations.¹⁷²

Because of this superiority of the full-CONUS slots, the Commission “prohibit[ed] any person with an attributable interest in DBS channels at one full-CONUS orbital location from acquiring an attributable interest in the full-CONUS channels now available at 110°[WL] without divesting its prior interest” when it adopted the rules for auctioning the orbital slots reclaimed from Advanced Communications Systems.¹⁷³ The Commission adopted that rule to encourage “the entry of a new full-CONUS DBS service that has the incentive to fully compete with full-CONUS DBS operators at other orbital locations.”¹⁷⁴ In adopting this one-time rule, the FCC sought “to foster rivalry among MVPDs by promoting rivalry within the DBS service.”¹⁷⁵

Pegasus recognizes, of course, that the Commission authorized both EchoStar and DIRECTV to acquire other DBS operators with either full-CONUS authorizations or

¹⁷² *In re Application of Direct Broadcasting Satellite Corp.*, Order, 11 FCC Rcd. 10,494, 10,498-99 ¶¶ 13-14 (I.B. 1996). *See also DBS Auction Order, supra*, at 9,727-32 ¶¶ 39-50. EchoStar has argued that even access to full CONUS locations is not sufficient to permit competition. Thus, in opposing the merger of DirecTV and Tempo, EchoStar claimed:

In view of these inefficiencies and less-accessible consumer offering, it seems at least possible that the motive underlying a “three-slot” plan could be to try to marginalize the operator using the remaining spectrum at those locations, pushing it to a niche strategy of product differentiation and preventing it from competing against cable operators head-to-head on prices. Such a result would compromise the cause of competition in the MVPD market, and the Commission should avoid it.

Petition to Deny filed by EchoStar Communications Corp. in File No. SAT-ASG-19990127-00014, at 4 (Mar. 5, 1999).

¹⁷³ *See DBS Auction Order, supra*, at 9,736 ¶ 62.

¹⁷⁴ *See id.*

¹⁷⁵ *See id.* at 9,737 ¶ 64 (stating that the “auction rule is designed to ensure that there is an opportunity for the quickest possible entry by an additional full-CONUS DBS system in order to increase the possibility of vigorous rivalry among MVPDs”).

spectrum at full-CONUS orbital locations.¹⁷⁶ However, in each of those cases, intra-DBS competition remained after the merger or acquisition because both EchoStar and DIRECTV remained significant DBS players. As such, the result was consistent with the policy goals that underlay the Commission's adoption of the one-time full-CONUS licensing restriction. With two DBS providers operating from full-CONUS locations, plus the added competition of cable service in many areas, MVPD competition was preserved and both DBS operators had the incentive to introduce new services, improve their use of spectrum and orbital slots, keep prices for both equipment and services low, and serve rural and other areas not fully served by cable. Those decisions do not support the proposition that one firm should control all the full-CONUS orbital locations.¹⁷⁷

Allowing this merger to proceed would be inconsistent with the sound, pro-competitive policies underlying one full-CONUS restriction adopted in the *DBS Auction Order*. It would destroy any rivalry or competition between the two dominant DBS operators; detract from incentives to improve service to DBS customers; reduce the prospects that rural homes that do not have access to cable (or are limited to out-of-date analog cable systems) will be served; and – because the merger will give one DBS

¹⁷⁶ See, e.g., *In re Applications of MCI Telecommunications Corp. and EchoStar 110 Corp.*, Order and Authorization, 15 Comm. Reg. (P&F) 1038, 1044-45 ¶ 21 (1999); *In re Tempo Satellite, Inc. and DirecTV Enterprises, Inc.*, Order And Authorization, 14 FCC Rcd. 7,946 (1999); *In re United States Satellite Broadcasting Co., Inc. and DIRECTV Enterprises, Inc.*, Order and Authorization, 14 FCC Rcd. 4,585 (1999).

¹⁷⁷ EchoStar has acknowledged that use of two of the full-CONUS slots is sufficient to permit effective competitive DBS service. As it stated in its Petition to Deny DIRECTV's application to acquire Tempo, "the Commission should not permit a single operator to use spectrum at all three full-CONUS orbital locations. The use of two adjacent full-CONUS slots allows an efficient and attractive MVPD offering...." Petition to Deny filed by EchoStar Communications Corp. in File No. SAT-ASG-19990127-00014, at 2 (Mar. 5, 1999).

operator control of all the full-CONUS slots – preclude the prospects of any new competitive entry by a “viable full-CONUS operator”¹⁷⁸ for the reasons the Commission itself so effectively articulated.¹⁷⁹

EchoStar and DIRECTV have not advanced any arguments which justify the Commission’s abandonment of this well-reasoned position, especially since, as demonstrated above, both DIRECTV and EchoStar can provide local-into-local service in 100 DMAs (or more) – as well as a full array of cable programming and advanced services – without the merger. As EchoStar itself has argued in other FCC proceedings, the Commission should not “allow a non-dominant MVPD to become dominant by acquiring additional DBS channels. Rather, the Commission should . . . prohibit such transactions where appropriate to protect against the likelihood of market-dominant behavior.”¹⁸⁰ That is exactly what the Commission should do here.

¹⁷⁸ *DBS Auction Order, supra*, at 9,736 ¶ 62. As EchoStar previously has recognized, in comments it filed regarding the affiliation of DBS operators and cable operators, “holding channels at more than one slot may be used as a strategy for precluding competition” due to the natural advantage offered by full-CONUS orbital locations over partial-CONUS locations. Revised Comments of EchoStar Satellite Corp. and DirectSat Corp. to the Notice of Proposed Rulemaking in IB Dkt No. 95-168 and PP Docket No. 93-253, at 44 (Nov. 21, 1995).

¹⁷⁹ The Commission has acknowledged that access to one of the full-CONUS orbital locations is essential if an entrant is to compete in the DBS business.

We recognize that if we allow EchoStar to acquire MCI’s authorization to operate 28 DBS channels at the 110 degrees W.L. orbital location, another firm with the intent of competing with cable operators is unlikely to enter the U.S. DBS industry. This likelihood arises from the fact that there will be few unused full-CONUS DBS channels left after this transaction, and those that are left, represent an amount of capacity that is likely to be insufficient to offer a competitive substitute to cable offerings.

In re Applications of MCI Telecommunications Corp. and EchoStar 110 Corp., Order and Authorization, 15 Comm. Reg. (P&F) 1,038, 1,044 ¶ 21 (1999).

¹⁸⁰ See Reply Comments of EchoStar Satellite Corp. and DirectSat Corp. to the Notice of Proposed Rulemaking in IB Dkt No. 95-168 and PP Dkt No. 93-253, at iii (Nov. 30, 1995). See also *id.* at 25 n.14 (advocating “restrictions on acquisition of DBS

Footnote continued on next page

B. Grant Of The Application Will Result In The Warehousing Of Orbital Locations And Spectrum Or The Loss of Orbital Slots

1. New EchoStar Will Have More Ka-Band Spectrum Than Possibly Needed In The Foreseeable Future, And Allowing The Merger To Proceed Will Result In Warehousing Of Spectrum, Contrary to FCC Rules

In addition to controlling all of the Ku-band full-CONUS orbital locations and most of the half-CONUS (wing) Ku-band DBS slots,¹⁸¹ EchoStar and DIRECTV

Footnote continued from previous page

channels . . . [applicable] to all MVPDs that may be subsequently found by the Commission to be dominant, whether they are large cable operators or not”).

¹⁸¹ EchoStar is authorized to use 21 DBS frequencies at 119°, 29 frequencies at 110°, for 50 full-CONUS frequencies, 24 DBS frequencies at 148° W.L. and 11 DBS frequencies at 61.5°. EchoStar also operates by STA 13 additional frequencies at 61.5° W.L. and sub-leases several of the remaining 8 frequencies at that location. DIRECTV is authorized to use 11 DBS frequencies at 119°, 3 at 110° and 32 at 101° W.L. EchoStar: See *Letter from Regina M. Keeney, Chief, Int’l Bureau, FCC, to Direct Broadcasting Satellite Corp.*, 13 FCC Rcd. 10,395 (1998) (authorizing channels 2-22 (even) at 61.5° W.L.); File No. SAT-STA-20010820-0076 (STA under which Echostar operates channels 1-23 (odd) and 24 at 61.5°); *In re Dominion Video Satellite, Inc.*, Order and Authorization, 14 FCC Rcd. 8,182 (1999) (authorizing Dominion to lease its assigned channels 25-32 at 61.5° from EchoStar); Sky Angel Press Release, *Dominion Joins DIRECTV & DISH Network in the High-Power DBS Service Arena; FCC Approves Dominion's Use of EchoStar III DBS Satellite*, May 17, 1999, available at, <http://www.skyangel.com/HTML%20Site/Body%20Pages/News/Releases/05171999.htm> (reporting that a portion of Dominion Video Satellite’s DBS frequencies have been sub-leased back to EchoStar for the approximate 12-year operating lifetime of the EchoStar III DBS satellite and that Dominion plans to launch its own satellite to use all of its DBS frequency); *In re Application of MCI Corp. and EchoStar 110 Corp.*, 15 Comm. Reg. (P&F) 1038 (1999) (28 channels at 110° W.L.); *Letter from Donald H. Gips, Chief, Int’l Bureau, FCC, to Direcstat Corp.*, 11 FCC Rcd. 16,465 (1996) (10 channels at 119° W.L.); *Letter from Donald H. Gips, Chief, Int’l Bureau, FCC, to EchoStar Satellite Corp.*, 11 FCC Rcd. 16,465 (1996) (10 channels at 119° W.L.); *In re Application of EchoStar DBS Corp.*, 12 FCC Rcd. 11,946 (1996) (24 channels at 148° W.L.). DirecTV: See *United States Satellite Broadcasting Co., Inc. and DirecTV Enterprises, Inc.*, 14 FCC Rcd. 4,585 (IB 1999) (5 channels at 101° W.L. and 3 channels at 110° W.L.); *In re Applications of Advanced Communications Corp. and Hughes Communications Galaxy, Inc.*, Memorandum Opinion and Order, 6 FCC Rcd. 2,269 (1991) (authorizing 27 channels at 101° W.L. and discussing earlier assignments); *In re Tempo Satellite, Inc. and DirecTV Enterprises, Inc.*, 14 FCC Rcd. 7,946 (I.B. 1999) (11 channels at 119° W.L.).

currently hold Ka-band authorizations for the following orbital locations from which service can be provided to CONUS:¹⁸²

Orbital Location	Licensee	Spectrum Authorized
83° W.L.	EchoStar	500 Mhz
99° W.L.	DIRECTV	1000 Mhz
101° W.L.	DIRECTV	1000 Mhz
103° W.L.	PanAmSat	1000 Mhz
113° W.L.	EchoStar	1000 Mhz
121° W.L.	EchoStar	500 Mhz
131° W.L.	DIRECTV	1000 Mhz
133° W.L.	PanAmSat	1000 Mhz

In addition to these authorizations, EchoStar has an equity interest in Wildblue Communications¹⁸³ which, through WB Holdings 1 LLC (“WB Holdings”),¹⁸⁴ is authorized to operate satellites at 109.2°WL and 73°WL¹⁸⁵ jointly with “KaStarCom. World Satellite LLC” (“KaStarCom”), an affiliate of Wildblue Communications.¹⁸⁶

¹⁸² For the purposes of this analysis, Pegasus is assuming that full-CONUS coverage can be achieved from 62°WL to 135°WL.

¹⁸³ See Application, Attachment D, at 2 (stating that, as of Mar. 2000, EchoStar had a 20% voting interest in WildBlue Communications).

¹⁸⁴ WB Holdings is managed by and is a wholly owned subsidiary of Wildblue Communications. See KaStar 109.2 Acquisition, LLC, Application for Transfer of Control, File No. SAT-T/C-20010108-00004, Ex. A, at 1 (Jan. 8, 2001).

¹⁸⁵ See *In re WB Holdings 1 LLC*, Order and Authorization, 16 FCC Rcd. 2,513 (I.B. 2001) (“*Second Round Ka-Band GSO Assignment Order*”) (modifying WB Holding 1 LLC’s license to launch and operate satellites at 73°WL and 109.2°WL); *In re KaStarCom. World Satellite, LLC*, Order and Authorization, 16 FCC Rcd. 14,389 (I.B. 2001) (authorizing KaStarCom to use 500 MHz at 73° W.L. and 109.2° W.L. through satellites jointly constructed and owned by Wildblue Communications).

¹⁸⁶ KaStarCom’s co-founders and principal owners are David Drucker and Walter Segaloff, who, along with various family members and related trusts, also founded Wildblue Communications and currently control in the aggregate a total of approximately 22% of its voting stock. See KaStarCom. World Satellite, LLC, Application to Construct, Launch and Operate a Geostationary Orbit Fixed Satellite Service in the Ka-Band, SAT-LOA-19980312-00018, at 43 and Exhibit D-2, at 1 (Dec. 22, 1997); KaStar 109.2 Acquisition, LLC, Application for Transfer of Control, File No. SAT-T/C-20010108-00004, Exhibit A, at 1 (Jan. 8, 2001).

KaStarCom is also separately authorized at 111°WL.¹⁸⁷ EchoStar also has an equity interest in and shares the 83° and 121° slots with CelSat America, Inc. (“CelSat”), which reportedly is in difficult financial straits and may not be able to construct.¹⁸⁸ Further, since EchoStar shares spectrum with CelSat, it is in a unique position to acquire the 500 Mhz assigned to CelSat if CelSat is unable to implement its satellite system.

As a result, New EchoStar could control between 8 and 11 Ka-band orbital locations – approximately one-third of the U.S. authorized Ka-band satellites capable of serving CONUS – substantially more than any other entity. This spectrum is in addition to the substantial Ku-band FSS capacity it will acquire from Hughes Electronics and PanAmSat, and the fleet of C-Band satellites owned by Hughes.¹⁸⁹ The transfer applicants have failed to demonstrate that it needs all this capacity to offer a viable broadband satellite service.

Indeed, New EchoStar’s acquisition of this spectrum is clearly inconsistent with the Commission’s policies against the warehousing of spectrum and orbital slots underlying Sections 25.140(e) & (f) of the Commission’s rules.¹⁹⁰ Section 25.140(e) provides that applicants for authorizations in the fixed satellite service only will be

¹⁸⁷ See *In re KaStarCom. World Satellite, LLC*, Order and Authorization, DA 01-1687, 2001 WL 876975 (I.B. 2001) (authorizing KaStarCom to use 111° W.L.).

¹⁸⁸ *Second Round Ka-Band GSO Assignment Order*, *supra*, at Appendix. See also *In re Celsat America, Inc.*, Order and Authorization, 16 FCC Rcd. 14,278, 14,278-79 ¶ 2 (I.B. 2001) (reporting that EchoStar DBS Corp. owns a 17.6% interest in Celsat).

¹⁸⁹ See Application, Attachment C.

¹⁹⁰ See also *In re Rulemaking to Amend Parts 1, 2, and 25 of the Commission’s Rules to Redesignate the 27.5-29.5 GHz Frequency Band, to Reallocate the 29.5-30.0 GHz Frequency Band, to Establish Rules and Policies for Local Multipoint Distribution and for Fixed Satellite Services*, 12 FCC Rcd. 22,310, 22,320, ¶ 24 (1997).

granted two orbital locations.¹⁹¹ Section 25.140(f) provides that existing licensees will be allowed additional orbital locations only if their existing facilities are “essentially filled” and that the applicant “has no more than two unused orbital locations for previously authorized but unlaunched satellites” in the band.¹⁹²

New EchoStar will violate these provisions. It will have six Ka-band authorizations, four more than sanctioned by the rules. These rule violations require a denial of the transfer application. Without the merger, both EchoStar and Hughes have already committed to deploy their Ka-band satellite systems in a timely manner. The transfer applicants have not advanced any public interest benefit of the merger that would counterbalance this rule violation or otherwise justify a waiver of the rule.

2. New EchoStar's Failure To Launch New Satellites Will Result In The Loss Of Ka-Band Orbital Slots

Finally, New EchoStar’s control of this enormous amount of spectrum, coupled with the high cost of building six satellites when competitive conditions will not necessitate incurring that expense, raises the real prospect that the United States will lose some of its International Telecommunications Union (“ITU”)-protected orbital locations. As the Commission is aware, under the ITU regulations, the currently authorized Ka-band satellite systems must be operational by June 2005 or other nations will enjoy the protection of the ITU registration system.

Given that New EchoStar is unlikely to use six satellites, rather than two or three, and the high probability that there will be insufficient near-term demand to fill those

¹⁹¹ 47 C.F.R. § 25.140(e).

¹⁹² 47 C.F.R. § 25.140(f).

satellites, New EchoStar could well decide that it no longer needs all six orbital locations and surrender some of its authorizations or fail to meet the necessary milestones. Indeed, the Application portends as much already.¹⁹³ At that point, the Commission will not be in a position to authorize additional satellites to begin operation by the ITU's Bring-Into-Use date for these orbital slots. Thus, mere delay by New EchoStar, which New EchoStar might argue was justified by the uncertainty surrounding the outcome of this proceeding, could jeopardize U.S. orbital slots currently protected by the ITU and foreclose additional competition by other U.S.-based satellite operators. The Commission cannot sanction this result by granting this transfer application.

VII. Notwithstanding The Transfer Applicants' Multiple Statements To The Contrary, It Is Clear That New EchoStar Aggressively Is Pursuing A Vertical Integration Strategy

In touting the public interest benefits of their merger, the transfer applicants said that “[t]he merger will also contribute to the diversity of independent programming voices, as it will create a significant multi-channel distributor that has no strategy of vertical integration with programmers.”¹⁹⁴ Less than two weeks after the Application was filed, on December 14, 2001, EchoStar and Vivendi – a Paris-based, international media conglomerate and major supplier of video programming – announced their “strategic alliance.” That announcement contravenes EchoStar’s proclaimed

¹⁹³ See Application at 45.

¹⁹⁴ Application at ii (bold emphasis in original; underlining added). See also Application at ii, 6, 42-43 (“[T]he proposed merger will not create the types of vertical relationships that raised concern in other transactions.”); Declaration of Dr. Robert D. Willig at 26-27.

independence from programming suppliers and directly contravenes what was said in the transfer application.¹⁹⁵

The Vivendi alliance makes clear that EchoStar is in fact pursuing a “strategy of vertical integration.”¹⁹⁶ Contemporaneously, Vivendi is acquiring USA Networks,¹⁹⁷ and EchoStar apparently is negotiating with Metro-Goldwyn-Mayer Inc. (“MGM”) to

¹⁹⁵ As the Commission recently has stated, “[v]ertical integration occurs where a video programming distributor has an ownership interest in a video programming supplier or vice versa.” *Eighth Annual Report, supra*, ¶ 156. In this connection, one industry observer noted: “For EchoStar, it is the first significant content alliance that could be useful in pursuing content-based strategies (as opposed to pure pricing strategies) in competing with cable. . . .” Blair Levin and Michael J. Balhoff, Legg Mason Equity Research *Industry Update: Telecom Regulation*, Dec. 17, 2001.

EchoStar officials almost certainly were aware of these impending, multi-faceted arrangements when the consolidated transfer application was filed on December 3, 2001 – just eleven days before the Vivendi deal was announced to the public. Thus, their decision affirmatively to disavow any vertical integration intentions on the brink of the Vivendi deal suggests that EchoStar was not forthcoming.

¹⁹⁶ For example, in EchoStar’s December 14, 2001 press release, Vivendi Chairman Messier stated: “With today’s announcement, Vivendi Universal is securing key access to consumers, as this ‘multi-dimensional’ transaction provides us with an important distribution system for our broad array of assets – from content to technology. This agreement is a foundation upon which we all intend to build even more value-creation opportunities for the benefit of our customers.” See Press Release, “EchoStar, Vivendi Universal Form Strategic Alliance to Offer New Programming, Interactive Televisions Services for Consumers,” Dec. 14, 2001, available at http://biz.yahoo.com/bw/011214/142044_1.html. See also Andy Pasztor, *EchoStar Chief Looks to Vivendi to Spark Growth in His Satellite-Broadcast Business*, WALL ST. J., Dec. 17, 2001 (“Vivendi’s move ‘serves as an endorsement’ of the ‘fundamental value’ of EchoStar’s growth plans and assures Mr. Ergen’s company [EchoStar] some ‘of the benefits of vertical integration’ through more favorable access to programming, according to Merrill Lynch analyst Marc Nabi. . . . In joining forces with Vivendi, *EchoStar is following the lead of other large media players determined to meld distribution and content.*”) (emphasis added).

¹⁹⁷ Shortly after the EchoStar/Vivendi deal was announced, Vivendi announced that it would purchase USA Networks for \$10.3 billion in stock and cash. See *Vivendi Signs 2nd Big Deal to Create Vertical Integration*, COMM. DAILY, Dec. 18, 2001. It is clear that the two Vivendi transactions are part and parcel of an overall vertical strategy: “‘Our strategy is clearly coming together,’ Vivendi Universal CEO Jean-Marie Messier said. ‘Combining with the same operational entity, VUE [Vivendi Universal Entertainment], USG [Universal Studios Group] and the other entertainment assets of USA creates a new U.S. major which will benefit from the full integration of TV and movies . . . with production and distribution.’” *Id.* (alteration in the original).

create an MGM-branded channel for EchoStar's DBS service.¹⁹⁸ It is thus clear that one of the principal benefits urged in support of the transaction has disappeared.

Given the DBS monopoly the merger would create, there is reason to wonder whether this vertical integration will cause additional public interest harms. Unfortunately, neither the Commission nor the public has been given the information that is essential to evaluating that issue. Specifically, the transfer applicants have failed to disclose the Annexes to the EchoStar/Vivendi Investment Agreement which set forth the substantive commercial terms of the "strategic alliance." Because those key agreements were neither publicly filed with the SEC nor submitted to the FCC, Pegasus filed a petition to suspend the pleading cycle in this proceeding until such time as all information about the Vivendi transaction was produced.¹⁹⁹ The sole purpose of that petition was to urge the Bureau to make certain that this proceeding is evaluated on as complete a record as possible. Unfortunately, the Bureau denied the petition, but in so doing it expressly noted that: "EchoStar, nonetheless, indicates that it will release this 'sensitive information,' *i.e.*, Annexes I through IV to the Investment Agreement, pursuant to the Protective Order in this proceeding."²⁰⁰ Notwithstanding that unambiguous statement, the transfer applicants have not supplemented the record with additional information about the EchoStar/Vivendi "alliance," and EchoStar refused Pegasus' request that they

¹⁹⁸ See Dan Cox, *Coming To A TV Near You; MGM Planning Cable Channel With EchoStar*, N.Y. POST, Jan. 11, 2002, at 34.

¹⁹⁹ See Pegasus Communications Corp. Petition to Suspend the Pleading Cycle, CS Dkt No. 01-348 (Jan. 14, 2002).

²⁰⁰ *Order Denying Pegasus Communications Corp.'s Petition to Suspend the Pleading Cycle*, CS Dkt No. 01-348, DA 02-178, 2002 WL 87554, n.9 (rel. Jan 24, 2002) ("FCC Pleading Cycle Order").

be made available under the terms of the protective order, by stating that EchoStar had no obligation to produce them.²⁰¹ When EchoStar finally complies with what it committed to do, Pegasus urges the Bureau honor its commitment to commence an additional pleading cycle so that interested parties may fully assess the impact of this transaction on the public interest.²⁰²

In light of these developments, the Commission cannot deem the absence of vertical integration, as asserted by the transfer applicants, to be a public interest benefit of this transaction.

²⁰¹ On January 25, 2002, Pegasus' counsel, in a letter to EchoStar's counsel, requested that these documents be provided pursuant to the Protective Order, to which EchoStar's counsel responded by letter dated February 1, 2002. See Attachments C-97 to C-98.

²⁰² See *FCC Pleading Cycle Order*, *supra*, ¶ 4 (“At such time [*i.e.*, when EchoStar provides additional information], if appropriate, we will initiate a new comment period to allow parties to submit additional or supplemental information.”). Moreover, in addition to the Annexes, EchoStar should produce (pursuant to the Protective Order) any definitive Commercial Agreements that have been executed. This obligation should continue until such time as this proceeding concludes (*i.e.*, Commercial Agreements executed subsequent to any production should be produced once they are completed).

CONCLUSION

For all of the foregoing reasons, Pegasus respectfully petitions the Commission to deny the pending consolidated transfer of control application in this proceeding.

Respectfully submitted,



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Dated: February 4, 2002

CERTIFICATE OF SERVICE

I, Robert M. Cooper, hereby certify that a true and correct copy of PEGASUS COMMUNICATIONS CORPORATION'S PETITION TO DENY was served on the following individuals by electronic mail on this 4th day of February, 2002.

Michael K. Powell
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